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Transcript Exhibit(s)

Docket #(s): W-01651B-99-0351

W-01651B-99-0406

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ALL CORP COMMISSION  
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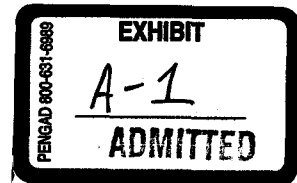
Arizona Corporation Commission

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BEFORE THE ARIZONA CORPORATION COMMISSION

2012 JAN 23 P 1:07

GARY PIERCE,  
Chairman

BOB STUMP,  
Commissioner

SANDRA D. KENNEDY  
Commissioner

PAUL NEWMAN,  
Commissioner

BRENDA BURNS,  
Commissioner

Arizona Corporation Commission

AZ CORP COMMISSION  
DOCKET CONTROL

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JAN 23 2012

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IN THE MATTER OF THE APPLICATION )  
OF VAIL WATER COMPANY FOR )  
AUTHORITY TO ISSUE PROMISSORY )  
NOTE(S) AND OTHER EVIDENCE OF )  
INDEBTEDNESS PAYABLE AT PERIODS )  
OF MORE THAN TWELVE MONTHS )  
AFTER THE DATE OF ISSUANCE. )

DOCKET NO. W-01651B-99-0351

IN THE MATTER OF THE APPLICATION )  
OF VAIL WATER COMPANY FOR A RATE )  
INCREASE )

DOCKET NO. W-01651B-99-0406

NOTICE OF FILING TESTIMONY

Attached is the Direct Testimony of Christopher Volpe filed on behalf of Vail  
Water Company.

Dated this 23rd day of January, 2012.

LEWIS AND ROCA

Michael F. McNulty  
Michael Hallam  
Lewis and Roca, LLP  
40 N. Central Avenue  
Phoenix, Arizona 85004  
Attorneys for the Vail Water Company

ORIGINAL and fifteen (15) copies  
of the foregoing filed this 23rd day of  
January, 2012 with:

LEWIS  
AND  
ROCA  
LLP  
LAWYERS

1 Arizona Corporation Commission  
2 Docket Control – Utilities Division  
3 1200 W. Washington Street  
4 Phoenix, Arizona 85007

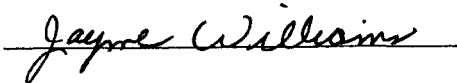
5 COPY of the foregoing hand-delivered  
6 this 23rd day of January 2012, to:

7 Janice Alward, Chief Counsel  
8 Charles Hains  
9 Legal Division  
10 Arizona Corporation Commission  
11 1200 W. Washington Street  
12 Phoenix, Arizona 85007

13 Steve Olea, Director  
14 Utilities Division  
15 Arizona Corporation Commission  
16 1200 W. Washington Street  
17 Phoenix, Arizona 85007

18 COPY of the foregoing  
19 mailed this 23rd day of January, 2012, to:

20 Jane Rodda, Administrative Law Judge  
21 Hearing Division  
22 Arizona Corporation Commission  
23 400 W. Congress St.  
24 Tucson, Arizona 85701

25   
26

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

GARY PIERCE, Chairman  
BOB STUMP  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF )  
VAIL WATER COMPANY FOR AUTHORITY )  
TO ISSUE PROMISSORY NOTE(S) AND )  
OTHER EVIDENCE OF INDEBTEDNESS )  
PAYABLE AT PERIODS OF MORE THAN )  
TWELVE MONTHS AFTER THE DATE OF )  
ISSUANCE. )

**DOCKET NO. W-01651B-99-0351**

IN THE MATTER OF THE APPLICATION OF )  
VAIL WATER COMPANY FOR A RATE )  
INCREASE )

**DOCKET NO. W-01651B-99-0406**

**DIRECT TESTIMONY OF  
CHRISTOPHER VOLPE  
ON BEHALF OF VAIL WATER COMPANY  
JANUARY 23, 2012**

**DIRECT TESTIMONY OF  
CHRISTOPHER VOLPE  
ON BEHALF OF  
VAIL WATER COMPANY  
JANUARY 23, 2012**

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**I INTRODUCTION AND QUALIFICATIONS**

**Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND TELEPHONE NUMBER.**

A. My name is Christopher ("Kip") Volpe. My business address is 1010 N. Finance Center Drive, Suite 200, Tucson, AZ 85710, and my business phone number is 520-571-1958, ext. 105.

**Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

A. I am employed by TEM Corp., a management company that performs management services for Vail Water Company ("Vail" or the "Company") under a service contract.

**Q. PLEASE DESCRIBE VAIL WATER COMPANY AND ITS BUSINESS.**

A. Vail is a private water company that provides water to approximately 3,900 customers in Pima County, Arizona.

**Q. PLEASE DESCRIBE YOUR PRIMARY RESPONSIBILITIES FOR VAIL.**

A. I am a Vice President of the Company and oversee the administration and operations of Vail.

**Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

A. To address the issues set forth in the Procedural Order dated December 15, 2011.

**II BACKGROUND INFORMATION**

**Q. IN DECISION NO. 62450, THE COMMISSION APPROVED A SURCHARGE AND HOOK UP FEES TO ALLOW VAIL TO PURSUE THE DIRECT USE OF WATER FROM THE CENTRAL ARIZONA PROJECT ("CAP"). WHY IS VAIL CONTINUING TO PURSUE THIS DIRECT USE?**

1 A. It was the common understanding in the year 2000, as it is today, that the preferred  
2 course of action with respect to CAP utilization is direct use of CAP within Vail's service  
3 area, rather than CAP recharge, at such time as direct use becomes feasible. Because  
4 Vail's service area is more than 40 miles from the CAP aqueduct, no one envisioned that  
5 the Company would be economically capable of building a stand-alone water  
6 transmission system to provide its customers with CAP water. Rather, it was anticipated  
7 that at some juncture, the CAP's largest customer, the City of Tucson, would expand  
8 eastwards until its delivery systems were sufficiently close to Vail's infrastructure that  
9 Vail could then extend its system to that of Tucson Water, the City's wholly-owned water  
10 utility.

11 As far back as the 1970s, the City of Tucson had envisioned becoming a  
12 wholesale CAP delivery utility, serving other water utilities in the Tucson valley.  
13 However, due to initial problems with the City's CAP treatment facility, Tucson Water  
14 did not wheel CAP water to anyone from 1975 until very recently, notwithstanding that  
15 its service area expanded dramatically over that period, and notwithstanding that its  
16 infrastructure became increasingly accessible to numerous utilities, including to Vail.

17 In 2008, the Mayor and Council of the City of Tucson and the Board of  
18 Supervisors of Pima County agreed to enter into a wide-ranging water policy planning  
19 exercise, reviewing the fundamental changes that would be needed in the Tucson valley  
20 to ensure the community's future. One goal of this planning exercise was enabling  
21 Tucson Water to become a CAP wheeling entity in the Tucson valley. In 2009, Tucson  
22 Water again pursued the difficult job of finding mutually-acceptable ways to become the  
23 entity that transmitted CAP water from the CAP aqueduct to various utilities around the  
24 Tucson valley. Finally, in June 2011, the City of Tucson and the Town of Oro Valley  
25 entered into an intergovernmental agreement for wheeling CAP water that Tucson

1 anticipates will serve as a model for providing similar services to other residential water  
2 utilities in eastern Pima County, including Vail.

3 Following these developments closely, officials from Vail contacted Tucson  
4 Water to ascertain the feasibility of entering into a similar wheeling agreement. The City  
5 of Tucson, having looked forward to serving in this capacity now for some 35 years, was  
6 strongly encouraging, and negotiations between Tucson and Vail began in earnest at that  
7 time. As a means of illustrating the new water policy regime in effect at Tucson Water,  
8 we asked Tucson Water to provide a position statement of its interest in becoming a  
9 wheeling entity for Vail, and were provided with the correspondence from Interim  
10 Director Andrew Quigley dated August 16, 2011, attached as Exhibit A.

11 When the Commission issued Decision No. 62450, Vail's CAP allocation was  
12 786 acre-feet per year. Since that time, Vail's customer base has grown dramatically.  
13 Vail is currently serving approximately 1,100 acre-feet per year and, in anticipation of  
14 future growth, has acquired rights to 1,857 acre-feet per year of CAP water. The benefit  
15 of delivering CAP water directly to Vail's customers is magnified by this increase in  
16 customers and projected future growth, and the corresponding increase in demand within  
17 Vail's service area.

18 **Q. PLEASE DISCUSS THE FINANCIAL ASPECTS OF THE CAP PROJECT FROM**  
19 **VAIL'S PERSPECTIVE.**

20 A. From the time the Commission approved the CAP fees in 2000 until October 2011, Vail  
21 has collected a total of approximately \$4.1 million. Over that same period, Vail has spent  
22 approximately \$2.7 million on expenses related to maintaining its rights to the CAP  
23 allocation with the ultimate goal of delivering CAP water directly to its service area. As  
24 a result, and including investment earnings, we have accumulated approximately \$1.9  
25 million of CAP funds for future expenses necessary to complete this project.



1           As required by Decision No. 62450, all of the money collected from CAP fees is  
2           kept in a separate account and can only be used for expenses related to the project. The  
3           bulk of the capital expenses for this project will be incurred over the next few years as we  
4           implement our plans to deliver the CAP water directly to our customers. This is precisely  
5           how the Commission envisioned the CAP fees working -- that is, Vail would accumulate  
6           funds over the first 10-12 years so it would have adequate funds available when the large  
7           capital expenses were incurred. Vail currently projects that all of the accumulated funds,  
8           as well as all additional CAP funds that we collect between now and 2015, will be  
9           required to complete this project and fund annual ongoing CAP and wheeling costs.  
10          Again, this is how the Commission envisioned Vail funding this project when it approved  
11          the fees in 2000.

12   **III   TESTIMONY REGARDING ISSUES SET FORTH IN PROCEDURAL ORDER**  
13   **DATED DECEMBER 15, 2011.**

14   **Q.   WHAT ARE VAIL'S CURRENT PLANS FOR THE DIRECT USE OF CAP**  
15   **WATER IN ITS SERVICE AREA?**

16   A.   Vail still plans to deliver CAP water to its customers by the end of 2015 as required by  
17          Decision No. 62450. Although the original order required the Company to have final  
18          plans by the end of 2010, that is not the critical deadline to the ultimate completion of this  
19          project. On November 8, 2011, Tucson Water's Interim Director Sandy Elder sent Vail a  
20          letter, attached as Exhibit B, outlining the steps that will need to be taken to finalize a  
21          wheeling agreement that will take effect in 2015. As evidenced by the letter, Vail and  
22          Tucson Water have taken significant steps and will continue to take significant steps  
23          toward adoption of a wheeling agreement to allow direct use of CAP water by Vail's  
24          customers.

1 **Q. WHAT ARE THE BENEFITS OF VAIL'S PLAN TO USE CAP WATER**  
2 **DIRECTLY?**

3 A. Direct use of Vail's CAP water will benefit its customers in several ways. First, it will  
4 secure a renewable supply of potable water, fortifying its assured water supply. Direct  
5 access to the CAP water will also enhance Vail's ability to provide an uninterrupted  
6 supply from a source with similar quality to groundwater. In addition to these service  
7 benefits, the direct use of CAP water should be less expensive for Vail's customers in the  
8 long term by maintaining compliance with the management plan of the Tucson Active  
9 Management Area ("AMA") by mitigating Vail's replenishment obligations instead of  
10 purchasing more costly CAGR credits. The project will also relieve pressure on  
11 aquifers in the Tucson AMA and benefit the entire state by firming Arizona's supply of  
12 Colorado River water.

13 **Q. WHAT IS VAIL'S POSITION WITH RESPECT TO REFUNDS?**

14 A. Although Vail, at the suggestion of Commission Staff, offered to refund the CAP  
15 surcharges collected in 2011, Vail does not believe that this is the best approach. As  
16 explained above, all of the money Vail collects as CAP fees must either be used on the  
17 CAP project or refunded at some later date. Any refunds the Commission requires now  
18 will threaten the viability of this beneficial project. At this point, with significant  
19 expenses looming over the next few years, Vail strongly encourages the Commission to  
20 allow Vail to continue collecting the CAP fees and to evaluate the necessity for a refund,  
21 if applicable, after the project is completed.

22 **Q. IS THE CONTINUED USE OF FUNDS FROM THE CAP SURCHARGE AND**  
23 **THE CAP HOOKUP FEES STILL THE BEST PLAN TO FUND DIRECT USE OF**  
24 **CAP WATER BY 2015.**

25 A. Yes.

1 **Q. IS DECEMBER 31, 2015 STILL AN APPROPRIATE DATE BY WHICH TO**  
2 **REQUIRE DIRECT USE?**

3 A. Yes.

4 **Q. DOES VAIL BELIEVE THAT PENALTIES ARE APPROPRIATE IN THIS**  
5 **SITUATION?**

6 A. No. Vail's customers have not been harmed by the failure to meet the deadline to file  
7 plans by December 31, 2010. In fact, Vail's customers have received a benefit by not  
8 paying CAP fees starting in November 2011 and continuing until a final decision in this  
9 proceeding. As noted above, the Company has always planned to meet the ultimate,  
10 critical deadline of Decision No. 62450 -- the direct delivery of CAP water by the end of  
11 2015.

12 **Q. HOW MUCH IN CAP FEES HAS VAIL LOST SINCE IT STOPPED**  
13 **COLLECTING THEM IN NOVEMBER?**

14 A. In November and December, Vail lost approximately \$18,000 in CAP surcharges and  
15 \$9,500 in hook up fees. That is approximately \$14,000 per month, and I expect it to be  
16 roughly the same amount each month until the Commission allows Vail to begin  
17 collecting the CAP fees again. Vail would request guidance from the Commission on  
18 this issue as soon as possible since it will never be able to recover these funds, and, as  
19 already explained, the loss of funds in Vail's CAP account threatens the viability of this  
20 important project.

21 **Q. PLEASE EXPLAIN VAIL'S POSITION WITH RESPECT TO EXTENDING THE**  
22 **DEADLINE FOR SUBMITTING FINAL PLANS TO THE COMMISSION.**

23 A. Vail requests an extension of this deadline until June 30, 2013. Vail takes the  
24 Commission's deadlines very seriously and very much regrets not meeting this deadline.

1 Vail now recognizes that it should have sought an extension prior to December 31, 2010.

2 As previously explained, it was not possible for Vail to provide "final plans" by  
3 December 31, 2010, due to Tucson Water's internal schedule for wheeling CAP water to  
4 other utilities. Vail explained the situation to Staff beginning in the spring of 2011 and  
5 has been working with Staff since that time in an attempt to comply with the  
6 Commission's order. As evidenced by the recent progress made with Tucson Water, Vail  
7 is confident that it will complete final plans by June 30, 2013, if not sooner, and still meet  
8 the original deadline of December 31, 2015 for direct delivery of CAP water to its  
9 customers.

10 Decision No. 62450 recognized that extensions of the December 31, 2010  
11 deadline might be appropriate upon a showing of good cause (see Conclusion of Law No.  
12 7). For all of these reasons, good cause does exist to extend this deadline until June 30,  
13 2013. Although the Company failed to meet the original deadline, a failure which it very  
14 much regrets, this failure is not a basis to discontinue the progress being made toward the  
15 very important and critical goal of providing direct use of CAP water to Vail's service  
16 area.

17 **Q. PLEASE DISCUSS VAIL'S CAP EXPENSES THAT ARE DUE IN 2012.**

18 A. Vail is scheduled to pay CAP approximately \$254,000 in 2012. The vast majority of this,  
19 approximately \$240,000, is due before Vail takes delivery of its annual CAP allocation.  
20 Delivery occurs in March, April, and May of each year. Payments for these deliveries are  
21 due as follows: \$75,500 on February 20th, \$89,500 on March 20th, and another \$75,500  
22 on April 20th. As a result, Vail respectfully requests that the Commission provide  
23 authorization for Vail to use these funds as soon as possible.

1 IV CONCLUSION

2 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

3 A. Yes.

## **EXHIBIT A**

August 16, 2011



**CITY OF  
TUCSON**  
TUCSON WATER  
DEPARTMENT

Christopher Volpe  
The Estes Company  
1010 N. Finance Center Drive, Suite 200  
Tucson, AZ 85710

Subject: Wheeling CAP Water to Vail Water Company

Dear Mr. Volpe:

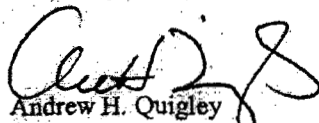
Thank you for approaching Tucson Water about wheeling a volume of the Vail Water Company CAP allocation, through our distribution system to your water system. As discussed, our extensive discussions with the Town of Oro Valley helped to identify the critical steps for building a foundation for a wheeling agreement. These steps include:

- Hydraulics analysis of our two water systems and identification of a connection point between them.
- Performing financial calculations of capital and operating costs plus the subsequent generation of a wheeling rate.
- Developing necessary legal documents.
- Construction of the necessary infrastructure to connect the two systems.

With respect to the recently completed wheeling agreement with Oro Valley, which was our first, this process took more than two years. A more complex agreement with the Pascua Yaqui Tribe took five years to complete. Based on the Oro Valley experience, we should be able to do much of it in a shorter timeframe; between six and twelve months.

Shortly, staff will be in contact with you to set up working meetings to begin building this foundation. I look forward to working with the Vail Water Company to complete a mutually beneficial agreement to move a volume of its CAP allocation off the canal, through the Tucson Water system and to the Company's service area.

Very truly yours,

  
Andrew H. Quigley  
Interim Director

AHQ/lr

cc: Richard Miranda, Deputy City Manager  
Sandy Elder, Deputy Director, Tucson Water



DIRECTOR'S OFFICE • P.O. BOX 27210 • TUCSON, AZ 85726-7210  
(520) 791-2666 • FAX (520) 791-3293 • TTY (520) 791-2639 • [www.cityoftucson.org](http://www.cityoftucson.org)



## **EXHIBIT B**





CITY OF  
TUCSON  
TUCSON WATER  
DEPARTMENT

November 8, 2011

Christopher Volpe  
The Estes Company  
1010 N. Finance Center Drive, Suite 200  
Tucson, AZ 85710

Subject: Wheeling CAP Water to Vail Water Company – Next Steps

Dear Mr. Volpe:

Thank you for your continued partnership in working with us to determine the requirements and most efficient solutions for Tucson Water (TW) to wheel Vail Water Company's (VWC) CAP allocation through our distribution system. As discussed at our last meeting on September 13, 2011, there are a number of items that still need to be addressed in order for TW and VWC to finalize a "wheeling design" with an ultimate goal of initiating wheeling in CY2015. These items are:

**- Financial – cost of service, wheeling rates, capital components, etc.**

Timeline on financial approval by Mayor and Council for standard water rates was provided after our last meeting. After the cost of service is determined in March 2012, we will have the necessary inputs to proceed with the detailed calculations to determine a wheeling rate to VWC.

POC: Belinda Oden

*Estimated Completion Date: 5/30/2012*

**- Power – determine initial cost and proposed escalation factor**

Parallel to the wheeling rate study, TW has already begun calculation of the power costs required to wheel an acre-foot of water to VWC. Preliminary calculations estimate that today's power cost to wheel VWC water is approximately \$160/AF. As in prior wheeling agreements, TW performs an annual adjustment on the actual power costs to wheel water.

POC: Cecilio Flores

*Estimated Completion Date: 10/31/11*

**- Hydraulic Analysis – determine infrastructure upgrades and interconnect location**

The hydraulic analysis performed to date shows adequate infrastructure capacity to wheel up to 2,000 AF of VWC's CAP allocation to the TW Houghton reservoir. In order to wheel the remaining distance to VWC's closest point of wheeling delivery location, upgrades to the Old Vail Tank site are needed along with a main extension.



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Re: Wheeling CAP Water to Vail Water Company – Next Steps  
10/27/2011  
Page 2

The construction of the booster upgrades and electrical service is currently planned as part of a developer financed project (Plan Number 096-2008) though no construction activity has taken place by the developer. If VWC were to construct the upgrades, an estimated financial requirement of \$200K is required. Additionally, approximately three miles of 12-inch main, with estimated cost of ~\$1.5M, is required to complete the connection between TW and VWC. Final details on transmission main alignment need to be identified.

POC: Richard Herran  
*Estimated Completion Date: 11/30/2011*

**- Finalize Wheeling Parameters – base or peak load, fire flow, etc.**

From prior discussions, it is understood that VWC will receive wheeled water under a base load scenario and that no fire flow will be provided though the wheeling interconnect. Confirmation of these parameters is lynch-pin to arriving at the wheeling rate and sizing infrastructure upgrades necessary to the wheeling.

POC: Sandy Elder and Joe Olsen  
*Estimated Completion Date: 11/30/2011*

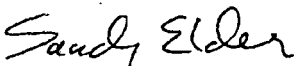
**- Wheeling Agreement – approval through respective governing bodies**

The final step to enacting a wheeling agreement between TW and VWC will be approval of the written wheeling agreement by the respective governing bodies. The wheeling agreement between Oro Valley and TW can serve as a template by which to fine tune based on the aforementioned parameters.

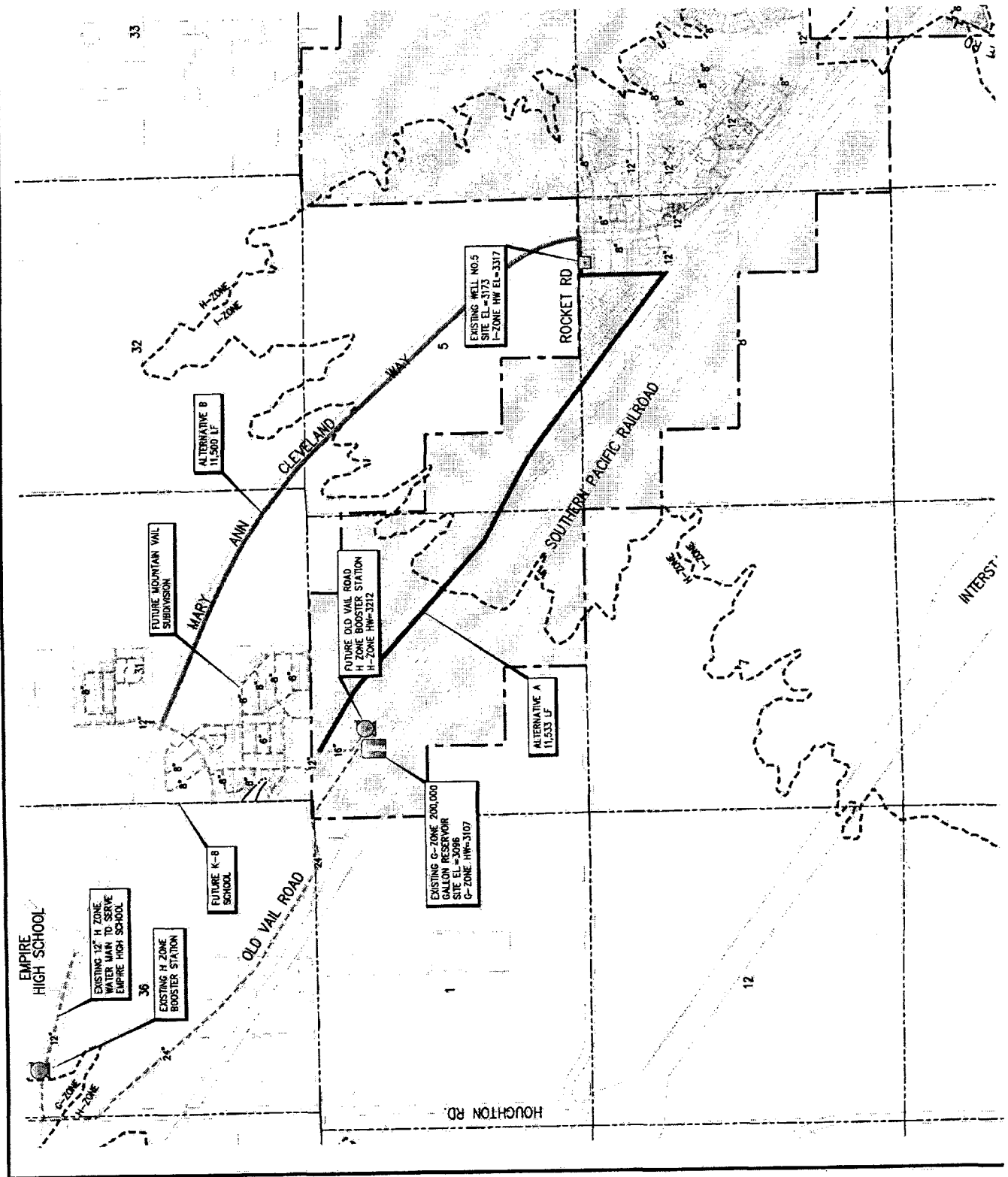
POC: Chris Avery  
*Estimated Completion Date: 6/15/2012*

We look forward to continuing to meet with you and your team to finalize the above items. Should you have any questions, please do not hesitate to contact me at 791-2666 or Joe Olsen at 837-2216.

Respectfully yours,

  
Sandy Elder  
Interim Director

JO/r



ORIGINAL

Vail Water Company  
1010 N. Finance Center Drive, suite 200  
Tucson, AZ. 85710



0000127353

Re: Decision No. 62450 Docket W-01651B-99-0351  
request for an extension of time

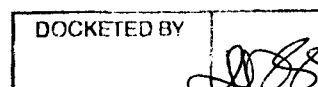
June 30, 2011

Mr. Brian Bozzo  
Compliance and Enforcement Manager  
Utilities Division  
Arizona Corporation Commission  
1200 W. Washington Street  
Phoenix, AZ 85007

Arizona Corporation Commission  
**DOCKETED**

JUL - 5 2011

In the above referenced Decision, Finding of Fact 25(f) orders that:



**"Final Plans for direct use of CAP water within Vail's service territory are to be submitted to the commission no later than December 31, 2010."**

The reasons for this request are because there wasn't a solution available to Vail Water Company (VWC) users until recently when Tucson Water started working with Oro Valley on its first "Wheeling Agreement". That agreement, which went to City Council on June 28, 2011 was to provide the template for future Wheeling Agreements with other providers such as Vail. There is no direct delivery option available to Vail other than this. Vail's recharge facility is in Marana, some 25 miles away. The Tucson area has virtually no direct CAP usage other than Tucson Water. That is why for the last 10 years Vail has researched different alternatives but always came back to the Wheeling Agreement being the only viable alternative. Until recently, Tucson Water did not entertain such agreements. Oro Valley is the first, which took a year to negotiate and is just now being considered for approval.

VWC has worked diligently toward compliance. Once Oro Valley is approved, the final plan for VWC should come shortly thereafter. VWC will immediately begin negotiations with Tucson Water. I have provided Brian Bozzo, in correspondence dated June 28, 2011, back-up material showing VWC efforts to secured a Wheeling Agreement, including emails to and from various officers of Tucson Water as well as a draft of Tucson Water's Wheeling Agreement with Oro Valley.

VWC is requesting an extension on the above requirement for Final Plans until November 30, 2011, taking into consideration that any agreement must be approved by Tucson Mayor and Council.

VWC is committed to direct delivery of CAP to its users. Thank you for your consideration

Sincerely,

Christopher T. Volpe  
Vice President

AZ CORP COMMISSION  
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2011 JUL - 5 11:38

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Cc: Carmel Hood-ACC

BEFORE THE ARIZONA CORPORATION COMMISSION

CARL J. KUNASEK

Chairman

JIM IRVIN

Commissioner

WILLIAM A. MUNDELL

Commissioner

IN THE MATTER OF THE APPLICATION OF  
VAIL WATER COMPANY FOR AUTHORITY  
TO ISSUE PROMISSORY NOTE(S) AND  
OTHER EVIDENCES OF INDEBTEDNESS  
PAYABLE AT PERIODS OF MORE THAN  
TWELVE MONTHS AFTER THE DATE OF  
ISSUANCE

DOCKET NO. W-01651B-99-0351

IN THE MATTER OF THE APPLICATION OF  
VAIL WATER COMPANY FOR A RATE  
INCREASE

DOCKET NO. W-01651B-99-0406

DIRECT

TESTIMONY

OF

JOHN A. CHELUS

UTILITIES CONSULTANT

UTILITIES DIVISION

DECEMBER 1, 1999

Vail Water Company

Docket No. W-1651A-99-0406 & W-1651B-99-0351

Page 9

Engineering has a number of concerns with the Company's replenishment proposal.

1. The replenishment district where Vail will recharge its CAP allocation is located 60 miles from the Vail CC&N. This will not provide any direct benefit to Vail customers. Over time, increased groundwater withdrawal coupled with increased surface water withdrawal may have a negative impact on the aquifer under Vail.
2. During the 1998 test year, the existing customers of Vail used 174.5 Acre-ft (56,903,000 gallons) of water. This means the CAP allocation is approximately 4.5 times larger than the amount of water the existing customers used in the test year. The existing customers should not have to pay for the entire CAP allocation.
3. The Company has not presented any long term plans to directly use its CAP allocation within the Company CC&N.

Engineering believes that it is important that the Company retains its CAP allocation as long as it is eventually delivered directly to Vail customers. This can only take place after an infrastructure is built within the Tucson AMA that will allow for the transport of CAP to the Vail CC&N. In the interim, Vail should be allowed to recharge its allocation at a remote location within the Tucson AMA and recover the associated costs. The costs related to the CAP allocation should be shared by all current and future ratepayers. In order to facilitate the Company's interim plan, Engineering proposes the following two-prong cost recovery mechanism:

1. Implementation of a CAP Service fee based on customer usage; and
2. Implementation of a CAP Hookup Fee for all new line extensions and subdivisions

#### Background Information

Vail CAP Allocation	786 acre-ft
Yearly Growth Rate	115 customers/year
Company Estimated Yearly CAP Costs	\$84,888 (\$37,728 Holding Costs, \$47,160 M & I)
Gallons Sold Test Year	56,903,000
Customers in Test Year	639

#### 1. Proposed CAP Service Fee

Engineering proposes that all customers should contribute to the utilization of CAP water. It recommends that a CAP service charge or fee per 1,000 gallons be charged. This service fee shall apply to all customers on the north system from the date of the order. Once the south and north systems are interconnected, the service fee would apply to all customers.

1 their water, so they're mining the water at a very  
2 fast rate. That water table affects this water table.  
3 So somewhere in the future, I think Vail customers  
4 will appreciate the fact that the allocation stayed  
5 here. But right now, I'm sure to a lot of the  
6 customers, they just can't even imagine that it's  
7 going -- that they're going to get any benefit from  
8 it.

9 HEARING OFFICER RODDA: Okay, thank you.

10 MR. SALLQUIST: Ms. Rodda, before Mr. Metli  
11 redirects, could I ask a couple of questions based  
12 upon your examination.

13 HEARING OFFICER RODDA: Okay.

14 MR. METLI: I have no objection.

15

16 FURTHER CROSS-EXAMINATION

17

18 Q. (BY MR. SALLQUIST) Mr. Chelus, you indicated  
19 that in the event the company needs to what I've heard  
20 for lack of a better term substitute some projects in  
21 the WIFA loan that it's your opinion that the company  
22 would then have to come back and seek yet another  
23 financing approval. Is that your testimony?

24 A. Either seek another financing approval or  
25 amend the current one.

1 Q. You're familiar with the critical timing that  
2 we've talked in this in getting things going and  
3 getting the Phase I construction and going in the  
4 Phase II and all?

5 A. Yes.

6 Q. Is there any reason that the Commission  
7 Staff, prior to the hearing officer issuing a  
8 recommended order and the Commission reviewing this,  
9 couldn't review those three or four substitute  
10 projects and provide their confirmation along with  
11 WIFA's that those are facilities that would qualify  
12 under the 819 so that we wouldn't have this delay?  
13 And I'm not sure if we know the precise timing of when  
14 the annexation funds could be used. Is there any way  
15 that you couldn't give blanket approval to \$1 million  
16 of projects, only 819 of which would be funded with  
17 WIFA funds?

18 A. Engineering Staff could look at other  
19 projects and approve those as optional projects, sure.  
20 And then as far as how the accounting and financing  
21 part of that goes, I don't handle that. But from  
22 engineering, I would have no problem with looking at  
23 some other projects, reviewing what they're going to  
24 be used for and putting them in as optional projects.

25 Q. These are relatively few projects, discrete



1 projects, and you're not reviewing engineering  
2 projects, you're just confirming that it's a health  
3 and safety type thing, it's not a growth thing, and it  
4 would be following the normal WIFA criteria.

5 A. Yes.

6 Q. Could that be done if the company would  
7 provide that information to Staff in the relatively  
8 near future? Is that something Staff engineering  
9 could turn around in a couple, three weeks?

10 A. Yes.

11 Q. Would you be willing to submit something to  
12 the Commission to confirm that there are additional  
13 substitute projects?

14 A. Yes.

15 Q. Following up on a question by the hearing  
16 officer regarding the time limitations where you say  
17 absolutely no extensions on this, you recognize that  
18 the Commission, even if they adopt at this point in  
19 time, if there were some extenuating circumstances,  
20 they could come back and extend the time frame?

21 A. Yes, anything's possible. The company could  
22 submit something and put it before the commissioners,  
23 and they could change the order.

24 Q. And you were in the hearing room yesterday  
25 when Mr. Rossi from DWR testified, were you not?

1 A. Yes.

2 Q. And when we were talking about the actual  
3 physical using of the CAP water in the boundaries of  
4 the Vail certificated area, you heard him discussing  
5 about several of the alternatives that might occur in  
6 the future as the infrastructure grows, including the  
7 possibility that we might co-op with Tucson on some  
8 joint treatment or transportation system?

9 A. Yes.

10 Q. So you do acknowledge that there are a number  
11 of variables that are not within the control of Vail  
12 to attempt to comply with the actual physical  
13 utilization of the water?

14 A. Yes.

15 Q. And would that be something that would -- I  
16 realize that you can't rule on it until you see it,  
17 but that's the kind of thing that should it occur and  
18 the company would be asking for an extension of the  
19 times that you're proposing would make some sense for  
20 Staff to support?

21 A. If it was virtually impossible and it was  
22 obvious that you couldn't get a connection through  
23 Tucson or something, I'm sure the company would apply  
24 for something.

25 Q. And the Staff could support it? We're not

1 talking about because we were dragging our feet, but  
2 it was basically something that was out of our  
3 control, but Staff could support an extension in that  
4 kind of a situation?

5 A. Yes.

6 MR. SALLQUIST: Thank you. I appreciate the  
7 opportunity to follow up.

8

9 REDIRECT EXAMINATION

10

11 Q. (BY MR. METLI) Mr. Chelus, if the company  
12 complies with your final plan and due to growth there  
13 is excess money in the deferred credit account over X  
14 amount of years, would Staff consider the company to  
15 -- allow the company to use the excess to install CAP-  
16 related projects?

17 A. Yes.

18 Q. Would these projects have to be part of the  
19 plan called for in items No. 6 and 7 on page 10 of  
20 your engineering report?

21 A. Yes.

22 Q. Now, if these projects were classified as  
23 projects for strictly growth, would it matter if  
24 engineering okayed them with respect to WIFA? Is that  
25 interrelated?

C. Volpe

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JUN 24 2004

AZ CORPORATION COMMISSION  
DIRECTOR OF UTILITIES

June 23, 2004

Arizona Corporation Commission  
Utilities Division Director  
1200 West Washington  
Phoenix, AZ 85007-2996

RE: Docket No. W-01651-99-0351  
Decision No. 62450  
Decision Compliance Status Report

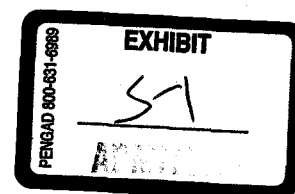
Dear Sir or Madam:

Regarding the action to submit annual reports beginning July 1, 2001 detailing the progress of plans to use CAP water directly in Vail Water's service territory and plans for actual construction of any necessary facilities, please be advised that we are investigating alternative plans to use the CAP water in our service territory but no physical action has taken place to date.

If you have any questions please do not hesitate to contact me at (520) 571-1958, extension 105 or via fax at (520) 571-1961.

Sincerely,

Christopher T. Volpe  
Vice President



BEFORE THE ARIZONA CORPORATION COMMISSION  
**DOCKETED**

APR 14 2000

CARL J. KUNASEK  
CHAIRMAN  
JIM IRVIN  
COMMISSIONER  
WILLIAM A. MUNDELL  
COMMISSIONER

DOCKETED BY

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IN THE MATTER OF THE APPLICATION OF  
VAIL WATER COMPANY FOR AUTHORITY TO  
ISSUE PROMISSORY NOTE(S) AND OTHER  
EVIDENCE OF INDEBTEDNESS PAYABLE AT  
PERIODS OF MORE THAN TWELVE MONTHS  
AFTER THE DATE OF ISSUANCE.

DOCKET NO. W-01651B-99-0351

IN THE MATTER OF THE APPLICATION OF  
VAIL WATER COMPANY FOR A RATE  
INCREASE.

DOCKET NO. W-01651B-99-0406

DECISION NO. 62450

OPINION AND ORDER

DATE OF HEARING: February 3 and 4, 2000

PLACE OF HEARING: Tucson, Arizona

PRESIDING OFFICER: Jane L. Rodda

APPEARANCES: Richard L. Sallquist, SALLQUIST & DRUMMOND, P.C., on behalf  
of Vail Water Company;

Monique Davis, in propria persona, Intervenor; and

Robert Metli, Staff Attorney, Legal Division, on behalf of the Utilities  
Division of the Arizona Corporation Commission.

**BY THE COMMISSION:**

On June 18, 1999, Vail Water Company ("Applicant" or "Company") filed with the Arizona Corporation Commission ("Commission") a rate application and a finance application. On July 19, 1999, the Commission's Utilities Division Staff ("Staff") filed a letter notifying the Company that its application met the sufficiency requirements outlined in A.A.C. R14-2-103 and classifying the Company as a Class C utility. By Procedural Orders dated September 28, 1999, and October 20, 1999, the Commission consolidated the matters. A hearing on the consolidated matter was held in Tucson, Arizona on February 3 and 4, 2000, pursuant to the schedule established by Procedural Order dated August 19, 1999. Prior to the commencement of the hearing, Monique Davis, a residential customer of Vail, was granted intervention.

**EXHIBIT**

S-2

ADMITTED

## Background

Vail provided water utility service to approximately 594 customers as of the end of the test year, December 31, 1998 ("TY"), in an area located southeast of Tucson in Pima County, Arizona. By November 30, 1999, the Company had 770 customers. Staff determined that the Company experienced an average annual increase of 115 customers over the past three years. The Company's current rates and charges were authorized in Decision No. 61110 (August 28, 1998), based on a test year ended December 31, 1996.

The Company operates two separate systems. At the time of the Engineering Staff Report, the north system served approximately 27 residential customers through Well No. 6. The south system served approximately 630 customers through Well No. 3. The Company is in the process of designing an interconnect between the north and south systems to increase reliability and provide another source of water to the south system. A 3,500 home planned community with golf course is planned in the area of the north system. There are smaller developments being planned in the southern portion of the system.

Engineering Staff reported that in the TY the Company experienced a water loss of 16 percent. Engineering recommended that the Company reduce its water loss to less than 10 percent within one year of this Decision, and that if water loss cannot be reduced to less than 10 percent, the Company must submit justification to the Utilities Division Director as to why doing so would not be cost effective.

In its finance application, Vail sought approval to borrow \$819,000 from the Water Infrastructure Finance Authority of Arizona ("WIFA") for the purpose of making needed upgrades to its water delivery system, including building a chlorination facility at Well No. 6 and connecting Well No. 6 to the southern portion of the system; upgrading two booster stations and rebuilding another; and construction of 6,700 feet of 12 inch distribution line to replace an inadequately sized 6 inch line. Vail also sought authority to convert \$150,000 in short term notes owing to shareholders into long term debt, payable over twenty years and to authorize additional long term borrowing from shareholders in the amount of \$143,000 to cover anticipated operating losses during the pendency of

1 the rate case proceeding. The Company subsequently reduced its financing request to the \$819,000  
2 WIFA loan and \$58,340 from shareholders.

3 In its simultaneously filed rate application, Vail claimed that in the TY it had a net operating  
4 loss of \$177,279, and that its revenues were not sufficient to support the proposed indebtedness  
5 needed to make the necessary improvements to its system. Initially, the Company sought rates that  
6 would generate total revenues of \$662,054 and result in a net operating income of \$121,555, which  
7 would produce an 11.61 percent rate of return on the Company's proposed adjusted rate base of  
8 \$1,046,978.

9 Staff determined that in the TY, Vail had adjusted total revenues of \$343,697 and an  
10 operating loss of \$117,504. Staff recommended a revenue level of \$433,920, which based on  
11 adjusted operating expenses of \$382,841, would yield operating income of \$51,079, a 37.9 percent  
12 rate of return on an adjusted original cost rate base of \$134,716. Staff recommended approval of the  
13 WIFA loan, but did not recommend approving additional long term borrowing from shareholders.  
14 Because of the Company's relatively small rate base, Staff recommended a revenue level to provide  
15 Vail with a Debt Service Coverage ("DSC") of 1.2, which is required to qualify for the WIFA  
16 financing. Staff's recommended revenue level is a 26.25 percent increase over adjusted TY revenue.<sup>1</sup>

17 In the course of the proceeding, Vail modified its revenue request, ultimately requesting a  
18 phased-in rate increase. In Phase 1, commencing approximately with the completion of the  
19 improvements to Well Nos. 6 and 3 in July 2000, the Company sought total revenues of \$501,800, an  
20 increase of 46 percent over Staff's adjusted TY revenues. In Phase 2, commencing approximately  
21 April 2001, with the completion of the remaining projects, the Company sought total revenues of  
22 \$548,685, an additional 11 percent increase. Overall, the Company sought a total increase in  
23 revenues of 57 percent.

24 A significant number of Vail's customers appeared at the public comment held prior to the  
25 hearing. Most of the customers who spoke were greatly concerned about the number of rate increases  
26

27 <sup>1</sup> Staff's recommendations include a CAP Hookup Fee of \$1,000 per new customer, but Staff did not treat these fees as  
28 revenue, but rather as a deferred credit. Vail agreed to the CAP Hook-up Fee but accounted for the expected fees as  
revenue. Consequently, it is unfair to compare Staff's recommended revenue increase with the Company's without  
considering the CAP Hook-up Fee.

1 they have experienced in recent years and were troubled by the current request which they believed  
 2 was too high. Some customers also complained about poor service quality. Customers also  
 3 questioned whether the proposed upgrades were needed to serve current customers or were being  
 4 instituted to accommodate future growth. During and subsequent to the public comment, the  
 5 customers presented the Commission with a petition signed by over 300 residents protesting the  
 6 amount of the increase.

### 7 Finance Application

8 The Company has requested authorization to borrow \$819,000 from WIFA for the following  
 9 capital improvements:

10 Rebuild Chlorination facility at Well No. 6	\$81,000
11 Rebuild Andrada Booster Station	\$85,000
12 Water Plant No. 2 – Booster station & transfer upgrade	\$161,000
13 Install 6,700 ft of 12" main to upgrade from 6"	\$192,000
14 Interconnect Well No. 6 with south system	\$300,000
	\$819,000

15 Staff considered these improvements to be necessary and important to improving the  
 16 reliability and quality of service to all customers. Staff also believed that the cost estimates were  
 17 reasonable.

18 At the hearing, the intervenor, a residential customer of Vail, questioned the Company  
 19 witnesses extensively about whether the improvements were necessary to provide reliable service to  
 20 existing customers or whether the improvements were required to permit growth. In particular, the  
 21 Intervenor questioned how much of the money needed for the required improvements should come  
 22 from current customers and how much from future growth customers.

23 Our Decision No. 62241 (January 12, 2000) which approved an extension of Vail's CC&N,  
 24 also approved an Annexation Participation Agreement between the Company and property owners  
 25 located within the extension area. The annexation Participation Agreement provided that the  
 26 extension area property owners would provide \$175,000 "to pay for upgrades to Well Nos. 3 and 6  
 27 and to provide trenching to loop the two wells plus the costs of any boosters, pumps, electrical and  
 28 water required to complete the upgrades." Thus, it appears that at least a portion of the improvements  
 to Well Nos. 3 and 6 that would have been provided with WIFA funds will be funded with monies



1 provided by property owners in the extension area.

2 At the hearing the Company argued that there are additional capital improvement projects that  
3 WIFA could and would fund in the event one of the approved projects receives funding from a  
4 different source. After the hearing, the Company submitted a list of four alternate projects to be  
5 funded with WIFA money.<sup>2</sup> Staff reviewed the projects which totaled \$302,800, and found them to  
6 be reasonable and acceptable improvements that would benefit Vail customers. Staff further opined  
7 that the cost estimates were reasonable.

8 A witness from WIFA testified that in the event a borrower did not utilize its full commitment  
9 from WIFA for the projects WIFA has committed to fund, whether that borrower could substitute  
10 other capital projects would depend on whether the additional projects were within the same priority  
11 level as the original projects. At this time, there is no evidence that WIFA would assign the same  
12 priority to the alternate projects submitted post-hearing by Vail. Nor was there testimony concerning  
13 which project(s) of the four would be funded if there was an extra \$175,000 available. It is not  
14 reasonable or prudent for the Commission to grant authority to borrow funds without knowing which  
15 projects will be funded. Consequently, we authorize Vail to borrow up to \$644,000 (\$819,000 -  
16 \$175,000) from WIFA for the purpose of constructing the facilities set forth in the Finance  
17 Application. There was testimony that these improvements are needed to maintain service quality for  
18 current customers but will also be required for future growth. We believe that funding these  
19 improvements through a combination of borrowing and contributions is an appropriate mix of  
20 funding sources from current and future customers.

21 The Company has also requested approval to borrow \$58,340 from shareholders for the  
22 acquisition of a truck and for capitalized engineering costs. Staff recommended that the Commission  
23 deny the \$58,340 loan request because based on the prospective WIFA borrowings of \$819,000, Staff  
24 believed the Company was too highly leveraged to warrant additional debt. Based upon our approval  
25 of a smaller WIFA loan, we will approve the shareholder loans in the amount of \$58,340. The funds  
26

27 <sup>2</sup> The alternate projects include a chlorination facility at Well No. 3 for \$31,000; telemetry control system at Well  
28 No. 3 and Well No. 2, Andrada booster station, Shasta Booster Station and Water Company Master Base Unit for \$73,000; Backup generator for transfer station generators for \$144,000, and 338- Zone Transfer/Booster Station 20% Allocation for \$54,800.

1 were utilized for capital expenditures which benefited the rate payers and the total combined debt and  
2 debt service obligation is lower than recommended by Staff. We will expect, however, that in the  
3 future, Vail seek Commission approval prior to issuing long-term notes, and we reiterate prior  
4 statements that it is not the policy of this Commission to approve debt financing for operating  
5 shortfalls.

6 The WIFA loan, with a 20 year term and interest rate of 6.25 percent, would have an annual  
7 debt service (principal, interest and reserve) of \$67,946. The shareholder loans, with 20 year terms  
8 and 10.25 percent interest rate, would have an annual debt service requirement of \$6,872. Staff  
9 recommended that a monthly surcharge per customer be set aside in a separate interest bearing  
10 account to be used solely for the purpose of servicing the WIFA debt. We concur with Staff. Based  
11 upon our authorized amount of WIFA financing, we will require that Vail deposit \$6.92 per customer  
12 per month in such account to be used for repaying the WIFA loan.

#### 13 Rate Application

14 The issues in the rate case involved: 1) the Company's proposal to include plant not yet  
15 constructed in rate base after Staff's verification that the plant was in service; 2) whether to include  
16 past Central Arizona Project ("CAP") expenses in rate base as a prepaid expense; 3) whether to  
17 calculate property taxes based on a forward looking or historic approach; 4) whether to include  
18 depreciation on the plant to be constructed in operating expenses; 5) how much of CAP operating  
19 charges should be approved on the income statement; and 6) how to calculate the Debt Service  
20 Coverage ratio used to determine required revenue levels.

#### 21 Rate Base

22 Vail requested that the Commission approve a rate increase, but defer its implementation until  
23 the plant to be constructed with WIFA financing is in service. Under the Company's plan, Phase 1  
24 rates would go into effect after the installation of the chlorination facilities at Well No. 6 and the  
25 completion of the interconnect of Well Nos. 3 and 6, and after Staff certified that the plant was used  
26 and useful. However, the Company's plan appears to determine the amount of plant and the rates in  
27 advance. Vail believed this approach would allow it to secure the WIFA financing but avoid the  
28 expense of another rate case in a short period of time for the purpose of including the new plant in

1 rate base. In addition, the Company argued, ratepayers are benefited because they don't pay the  
2 increased rates until the new plant is in service and the phase-in approach lessens the immediate  
3 burden on current rate payers. The Company also sought approval of the depreciation associated  
4 with the yet to be built plant in operating expenses.

5 As its final position, Vail requested a total Rate Base of \$1,026,474. The Company's request  
6 included \$2,979,430 in gross plant in service, which included Phase 1 plant of \$353,522 and Phase 2  
7 plant of \$466,479. The Company also sought to include Prepaid CAP Water Rights of \$70,188 and  
8 an Allowance For Working Capital of \$40,728.

9 Staff recommended a rate base of \$134,716, which in pertinent part would be comprised of  
10 gross utility plant of \$2,160,430, and Allowance For Working Capital of \$38,158. The Company and  
11 Staff agreed on figures for accumulated depreciation (\$500,987), net Contributions In Aid of  
12 Construction ("CIAC") (\$183,005), Advances in Aid of Construction (\$1,341,985) and Meter  
13 Deposits (\$37,895). The major difference between Staff and the Company is, of course, the inclusion  
14 of the yet to be constructed plant in Rate Base. The difference in the Allowance of Working Capital  
15 is due to the differences in the Company's proposed and Staff's recommended operating expenses.

16 Staff opposed the Company's proposal because it departs from the traditional rate-making  
17 approach of an historic test year used by the Commission. Staff recommended that the Commission  
18 approve the WIFA financing and recommended rates that would produce sufficient revenues that in  
19 Staff's opinion would permit the Company to qualify for the WIFA loan. Consistent with its  
20 recommendation not to include the WIFA plant in rate base, Staff did not recommend including the  
21 related depreciation expense in operating expenses.

22 Staff also opposed the Company's inclusion of Prepaid Water Rights in rate base because  
23 there was no benefit to ratepayers in the years when the expense was incurred. Furthermore, Staff  
24 asserted, the Company's CAP allocation of 786 acre feet is substantially higher than the current  
25 demand for water. Although it did not include the Prepaid Water Rights in rate base, Staff did allow  
26 amortization of this expenditure over twenty years.

27 We concur with Staff's treatment of the proposed plant to be constructed with WIFA  
28 financing. The Commission has historically dealt with the issue of providing sufficient revenue for

1 new plant construction by approving the financing and required revenue and then making the rate  
2 increase subject to refund in the event the plant is not installed within a reasonable time period. We  
3 do not see a need to deviate from that approach in this case. Furthermore, Staff's approach is the  
4 more financially sound. Although increased rates will be effective a few months earlier, the rates we  
5 approve herein will provide the funds needed to repay the WIFA debt and we will not have to address  
6 the question in the future of what happens if the Company has not constructed the plant as quickly as  
7 it anticipates, or the expected costs differ from current estimates. Moreover, there is no evidence that  
8 WIFA would agree to release funds to make the needed improvements in advance of the rates to  
9 make repayments being in place.

10 We also concur with Staff's position concerning Prepaid Water Rights for the same reasons  
11 Staff advanced. Finally, based on our approval of operating expenses, as recommended by Staff, we  
12 determine the correct level of Working Capital using the formula method to be \$38,158. As a result,  
13 we approve an OCRB of \$134,716.

#### 14 Revenue and Expenses

15 Vail and Staff concurred that in the TY, Vail's present rates yielded metered sales of  
16 \$340,358 and other operating revenue of \$3,341, resulting in total operating revenue of \$343,697.  
17 The Company requested total operating revenue of \$548,685.<sup>3</sup> In its final position, Staff  
18 recommended rates that would produce total operating revenue of \$433,920. Staff also recommended  
19 that new customers be assessed a \$1,000 fee to be applied toward the Company's CAP costs. Staff  
20 recommended that the CAP Hook-up Fee be treated as a deferred credit. Vail agreed to the CAP  
21 Hook-up fee, but believed that it should be accounted for as revenue.

22 Vail has accepted a number of Staff's adjustments to operating expenses, however, the parties  
23 did not agree on the amount of CAP expenses, property taxes, or depreciation.

#### 24 CAP Expenses

25 Vail has a CAP allocation of 786 acre feet for a cost of \$84,888 per year. In past years, the  
26 Company has not been allowed to recover the costs of its CAP allocation from ratepayers because the  
27

28 <sup>3</sup> In rejecting the Company's proposal to include not yet built plant in rate base, we do not need to consider the Company's phased-in rate increase.

1 Commission has not considered the allocation "used and useful" to customers. The Company had  
2 been unable to use its CAP allocation because there is no means for delivering the allocation from the  
3 CAP facilities to Vail's service territory on the other side of Tucson. Vail proposes to join a  
4 replenishment district to receive credits for its CAP allocation, which it can then use to withdraw  
5 groundwater from a designated well in its service area. The CAP water will be recharged at a  
6 location 60 miles from Vail, but within the same Active Management Area ("AMA"). According to  
7 the Company, the water will initially serve existing customers north of Colossal Road as well as  
8 provide backup water for a planned golf course.<sup>4</sup> The recharge program will also provide the  
9 necessary Assured Water Supply ("AWS") designation for a development of 3,300 homes, a high  
10 school, 110 acres of commercial development and 40 acres of industrial development.

11 Staff believed that it is important for Vail to retain its CAP allocation as long as it is  
12 eventually delivered to Vail customers. This can only happen after an infrastructure is built within  
13 the Tucson AMA that will allow for the transport of CAP water to the Vail service territory. In the  
14 interim, Staff believed that Vail should be allowed to recharge its allocation at a remote location  
15 within the Tucson AMA and recover the associated costs.

16 Because the Company's CAP allocation is greater than the water currently being utilized by  
17 its customer base, Staff opined that current customers should not be charged the entire CAP expense  
18 of \$84,888. Because current customer demand amounts to approximately 23.81 percent of the CAP  
19 allocation, the Company should only be allowed to recover that percentage, or \$19,277, of the  
20 expense from current customers by means of a CAP Service Fee based on customer usage. Under  
21 Staff's recommendation, the balance of the annual CAP costs, or \$61,681, would be recovered by  
22 means of a CAP Hookup Fee for all new line extensions and subdivisions.

23 Staff recommended the Commission approve a CAP Service Charge of \$0.32 per 1,000  
24 gallons of usage. The CAP Service Charge would apply to all customers on the north system from  
25 the date of the Order, and apply to all customers once the north and south systems are interconnected.  
26 Staff recommended that the CAP Service Charge be segregated in an interest bearing account and  
27

28 <sup>4</sup> The golf course will normally use surface water not owned by the Company.

1 used solely for the purpose of paying CAP holding and M & I expenses. Under Staff's proposal,  
2 when Vail pays its CAP allocation, payment must be tendered from the CAP cash account and the  
3 Company will not be allowed to expense more than \$19,277 on its income statement each year.

4 Staff also recommended a CAP Hook-up Fee that would apply to all new subdivision and line  
5 extension agreements. Staff recommended twelve conditions on the implementation of the Hookup  
6 Fee. One of the recommendations was that the funds received from this fee should be deposited into  
7 the segregated CAP account. Under Staff's plan, the funds from the CAP Hook-up Fee should be  
8 booked as a deferred credit. According to Staff, the treatment of the hook-up fee as a deferred credit  
9 will allow a mechanism for tracking the fees. Staff did not recommend that all of the CAP expenses  
10 be recovered on the income statement and believed that for purposes of matching revenue and  
11 expenses, the CAP Hook-up Fees should not be treated as revenue. Staff proposed a CAP Hook-up  
12 Fee schedule that ranged from \$1,000 for a 5/8 inch meter to \$250,000 for a 12 inch or larger meter.

13 The Company accepted the amount of Staff's proposed CAP Hook-up Fee, but disagreed with  
14 Staff's proposal that the CAP Hook-up Fee be booked as a deferred credit. Vail argued that neither  
15 the revenue from the hook-up fee, nor the expense of the purchased water, is a deferred credit. The  
16 Company also asserted that accounting for the Hook-up Fee as a deferred credit was an unnecessary  
17 accounting nightmare. Vail thought that Staff's only justification for treating the fees as a deferred  
18 credit was to avoid possible over-earning. Vail argued that Staff could bring the Company in for rate  
19 review if the Company does over-earn. Under the Company's proposal, the CAP Hook-up Fees  
20 would be treated as revenue and the entire CAP Expense would be allowed to be recovered in  
21 operating expenses.

22 We believe that the more reasonable approach is to treat the CAP Hook-up Fee as revenue  
23 when it is received. As a result, the entire \$84,888 CAP expenses is allowed as an expense. Of this  
24 amount, approximately \$19,277 will be recovered from ratepayers by means of the \$.32 per 1,000  
25 gallon CAP Service Charge, \$3,930 from the farm using the CAP allocation, and the remaining  
26 approximate \$62,000 by means of the CAP Hook-up Fees as Staff proposed. All funds received as a  
27 result of the CAP Service Charge and the CAP Hook-up Fee will be deposited in an interest bearing  
28 segregated account and used solely for CAP-related expenses. In the event the Company receives

more than \$84,888 in any year from any combination of the foregoing, the funds will remain in the segregated account and may be utilized for capital projects related to developing a delivery system for the direct use of CAP water in Vail's service territory, as contemplated by Staff, or will be refunded to customers. By segregating the funds and designating that they be used solely for CAP-related expenses and capital items, Staff's concerns about potential over-earning should be alleviated. As a further control, we will require Vail to submit annual reports commencing January 31, 2001, with the Director of the Utilities Division, detailing all deposits and expenditures from the CAP account. If in Staff's or Vail's opinion, the amounts accumulating in the CAP account are excessive, either Staff or Vail may request the Commission order the refund of the excess amounts to Vail's customers and may request an adjustment of the CAP Service Charge Fee or CAP Hook-up Fee. We also adopt Staff's conditions on the implementation of the CAP Hook-up Fee as delineated in the Engineering Staff Report.

### Depreciation

Because we are accepting Staff's position concerning the amount of plant in rate base, we adopt Staff's Depreciation Expense amount of \$48,327. The Company's proposed Depreciation Expense was based upon the assumption that the not-yet-built plant would be included in rate base.

### Property Taxes

Vail advocated that Property Tax Expense should be determined on a prospective basis using the Department of Revenue calculation methodology and based upon projected plant and revenue. Staff argued that the Property Tax Expense should be based upon the most recent property tax bill, in this case the 1999 bill in the amount of \$20,609. Vail proposed a Property Tax Expense of \$38,541 which was based upon projected plant balances, including plant to be financed with the WIFA loan and which is not yet constructed. Vail's plant balances are too speculative at this time to be utilized in the calculation of Property Tax Expense. Consequently, we adopt Staff's recommended Property Tax figure of \$20,609.

### Revenue Requirement and Rate Design

Staff and the Company agreed that a revenue level that would produce a DSC of 1.2 is appropriate in this case. They disagreed, however, on how to calculate the DSC ratio. Vail argued

that the DSC calculation should include meter deposit refunds and repayment of Advances in Aid of Construction. Staff did not include these obligations in its calculation because it believed that to do so would violate the standard that rates should only reflect the cost of service and because to recover 1.2 times the advance payments would negate the purpose of the advances as a cost-free source of capital. We agree with Staff, for the reasons stated, that these obligations should not be included in the DSC calculation. We are concerned, however, that Vail have sufficient cash flow to meet its legal obligations. Therefore, we will provide revenues sufficient to provide a DSC of 1.4.

We calculate Vail's revenue requirement as follows:

Debt Service Requirement	\$ 74,818
	• <u>1.4</u>
	\$104,745
Less Depreciation and Amortization	<u>\$ 52,021</u>
Operating Income	\$ 52,724
Operating Expenses	<u>\$448,452</u>
Required Revenue	\$501,176

The rates and charges we approve herein produce total revenues of \$497,246, as follows:

Metered Water Sales	\$359,557
Miscellaneous Revenues	3,341
CAP Service Charge	19,277
CAP Recharge Income	3,930
CAP Hook-up Fees	62,000
WIFA Surcharge	<u>53,132</u>
Total Revenues	\$501,237

\* \* \* \* \*

Having considered the entire record herein and being fully advised in the premises, the Commission finds, concludes, and orders that:

#### FINDINGS OF FACT

- On June 18, 1999, Vail filed with the Commission a rate application and a finance



1 application.

2 2. On July 19, 1999, Staff filed a letter notifying the Company that its application met the  
3 sufficiency requirements outlined in A.A.C. R14-2-103 and classifying the Company as a Class C  
4 utility.

5 3. By Procedural Orders dated September 28, 1999 and October 20, 1999, the  
6 Commission consolidated the matters.

7 4. A hearing on the consolidated matters was held in Tucson, Arizona on February 3 and  
8 4, 2000, pursuant to the schedule established by Procedural Order dated August 19, 1999.

9 5. Prior to the commencement of the hearing, Monique Davis, a residential customer of  
10 Vail, was granted intervention.

11 6. At the end of the TY, Vail provided water utility service to approximately 594  
12 customers. As of November 30, 1999, the Company provided service to approximately 771  
13 customers.

14 7. In its finance application, Vail requested authority to borrow \$819,000 from WIFA for  
15 the purpose of constructing necessary upgrades to its system. The Company also requested authority  
16 to issue long-term notes to shareholders in the amount of \$58,340 for the purpose of financing the  
17 purchase of a new truck and for capitalized engineering costs.

18 8. The Company requested approval of rates that would generate total revenues of  
19 \$548,685, to be phased in over approximately one year.

20 9. The Company requested authorization to borrow \$819,000 from WIFA to finance  
21 necessary system improvements including a chlorination facility at Well No. 6, rebuilding and  
22 upgrading boosters, the installation of 6,600 feet of 12 inch main to replace under-sized 6 inch main,  
23 and the interconnection of Well No. 6 with the south system.

24 10. Staff considered the proposed improvements to be necessary and important to  
25 improving the reliability and quality of service to all customers, and also believed that the cost  
26 estimates were reasonable. Staff recommended approval of the WIFA loan in the amount of  
27 \$819,000.

28 11. Staff recommended that the shareholder loans not be approved because with the

1 proposed \$819,000 WIFA loan, Staff believed the Company would be too highly leveraged.

2 12. In Decision No. 62241 (January 12, 2000) the Commission approved an extension of  
3 Vail's CC&N and approved an Annexation Participation Agreement between Vail and the property  
4 owners in the extension area. Pursuant to the Annexation Participation Agreement, the extension  
5 area land owners would provide \$175,000 to pay for upgrades to Well Nos. 3 and 6 and to provide  
6 trenching to loop the two wells plus the costs of any boosters, pumps, electrical and water required to  
7 complete the upgrades.

8 13. The improvements to Well Nos. 3 and 6 and the looping of the system that are going  
9 to be financed by the property owners in the recent extension area are some of the same  
10 improvements for which the Company has sought financing from WIFA.

11 14. It is reasonable and prudent to reduce the amount of funds borrowed from WIFA by  
12 the amount of funds received pursuant to the Annexation Participation Agreement.

13 15. In light of the reduced WIFA borrowing, it is reasonable and prudent to approve the  
14 shareholder loans in the amount of \$58,340.

15 16. Vail's current rates and charges produced adjusted gross revenues of \$343,697, which  
16 in conjunction with operating expenses of \$461,201, produced an operating loss of \$117,504 during  
17 the TY.

18 17. Vail's OCRB is determined to be \$134,716.

19 18. Vail waived the filing of a reconstruction cost new rate base, and as a result, its Fair  
20 Value Rate Base ("FVRB") is the same as its OCRB.

21 19. Under the circumstances a total revenue requirement premised on a DSC of 1.4 is just  
22 and reasonable.

23 20. Operating income of \$52,724 is required to yield a DSC of 1.4.

24 21. Operating income of \$52,724 results in a 39.1 percent rate of return on FVRB.

25 22. Vail's total revenues must increase \$157,540 over adjusted TY revenues to produce  
26 operating income of \$52,724.

27 23. The rates and charges approved herein increase the average monthly residential bill  
28

23.4 percent, from \$42.52 to \$52.48.<sup>5</sup>

24. Vail is in full compliance with the regulations of the Arizona Department of Environmental Quality, current with its property taxes and in compliance with Commission filing requirements and Orders.

25. Staff recommended approval of, and Vail agreed to, a CAP Hook-up Fee to be applied to new hook-ups under the following conditions:

- a. The tariff would apply to all new subdivisions and line extension agreements that are approved for the north system from the end of the 1998 TY forward. Once the interconnection is completed between the north and south systems, the tariff would apply to all new subdivisions and line extension agreements in the combined north and south systems;
- b. Vail must be recharging Cap water within 6 months of this Decision;
- c. All CAP Hook-Up Fees and CAP Service charges are to be placed in a separate interest bearing account;
- d. Revenue collected from the CAP Hook-up Fee and CAP Service Charge can only be used for payment of the CAP holding fee and Municipal and Industrial costs;
- e. The CAP Service Charge shall be identified as a separate line item charge on the customer bill;
- f. Final plans for the direct use of CAP water within Vail's service territory are to be submitted to the Commission no later than December 31, 2010;
- g. Vail must directly use the CAP allocation within its service territory by December 31, 2015;
- h. No time extensions will be allowed for any reason;
- i. Vail shall submit annual reports to the Utilities Division Director detailing the progress of plans to use CAP water directly in its service territory and plans for actual construction of any necessary facilities. The reports shall be submitted each July 1, beginning in 2001;
- j. If Vail does not comply with either of the timeframes in f or g, all CAP charges will cease at that time and any monies remaining in the CAP account shall be refunded in a manner to be determined by the Commission at that time;

<sup>5</sup> For comparison, the Company's proposed rates would increase the average monthly residential bill 36.7 percent, from \$42.52 to \$58.15, and Staff's recommended rates would increase the average monthly residential bill by 23 percent, from \$42.52 to \$52.29.

- k. The Commission shall allow Staff to automatically impose fines and/or other sanctions against Vail if the timeframes in item f or g are not met;
- l. If Vail does not comply with the timeframes in items f or g and it sells its CAP allocation, any net profit shall be distributed to the customers in a manner to be determined by the Commission; and
- m. Vail should submit annual reports regarding the amount of CAP Hook-up Fee and CAP Service Fees collected. The reports should be submitted by each January 31 and cover the previous calendar year. The first report should be submitted by January 31, 2001, and should contain the following information:
  - i. The name of each entity paying a CAP Hook-up Fee;
  - ii. The amount of CAP Hook-up Fee each entity paid;
  - iii. The amount of CAP Service Charge collected;
  - iv. The balance in the CAP trust account;
  - v. The amount of interest earned in the CAP trust account;
  - vi. The amount of money spent from the CAP trust account; and
  - vii. A description of what was paid for with monies from the CAP trust account.

26. In the TY, Vail suffered a water loss of 16 percent, which is higher than the recommended maximum rate of 10 percent. Staff recommended that the Company reduce its water loss to less than 10 percent within one year of this Decision, and that if water loss cannot be reduced to less than 10 percent, Vail must submit justification to the Director of the Utilities Division as to why doing so would not be cost effective.

27. Staff recommended that each month Vail deposit a monthly WIFA surcharge per customer in an interest bearing account to be used solely for the purpose of servicing the WIFA debt. Based upon our authorization to borrow \$644,000 from WIFA, Vail shall collect a WIFA surcharge of \$6.92 per customer per month (\$67,946/818 customers).

28. It is reasonable that the WIFA surcharge approved herein be deposited in a segregated interest bearing account and be interim and subject to refund in the event Vail fails to make the capital improvements set forth in its finance application by September 1, 2001.

29. Staff further recommended a provision be included in the Company's tariff to allow for the flow-through of all appropriate state and local taxes as provided for in A.A.C. R14-2-409(D)(5).

#### CONCLUSIONS OF LAW

1. Vail is a public service corporation within the meaning of Article XV of the Arizona

1 Constitution and A.R.S. §§40-250, 40-251, 40-301 and 40-302.

2 2. The Commission has jurisdiction over Vail and the subject matter of this proceeding.

3 3. Notice was provided as required by law.

4 4. The rates and charges approved herein below are just and reasonable and should be  
5 adopted.

6 5. The proposed WIFA financing in the amount of \$644,000 and shareholder loans in the  
7 amount of \$58,430 are for lawful purposes within Vail's corporate powers, is compatible with the  
8 public interest, with sound financial practices, and with proper performance by Vail of service as a  
9 public service corporation, and will not impair Vail's ability to perform that service.

10 6. The financing approved herein is for the purposes stated in the application and is  
11 reasonably necessary for those purposes, and such purposes are not, wholly or in part, reasonably  
12 chargeable to operating expenses or income.

13 7. Staff's recommendations set forth in Findings of Fact Nos. 25, 26, 27 and 29 and  
14 Findings of Fact No. 28 are reasonable, except that paragraph 25k is not warranted and pursuant to  
15 paragraph 25d, funds collected from CAP Hook-up Fees may be used for CAP-related capital  
16 projects; and paragraph 25h should be modified to provide no time extensions will be allowed absent  
17 a showing of good cause.

### 18 ORDER

19 IT IS THEREFORE ORDERED that Vail Water Company is hereby authorized and directed  
20 to file with the Commission on or before April 28, 2000, a revised rate schedule setting for the  
21 following rates and charges:

#### 22 MONTHLY SERVICE CHARGE

23 5/8 x 3/4 Inch Meter	\$ 13.18
3/4 Inch Meter	21.00
24 1 Inch Meter	40.50
1 1/2 Inch Meter	89.20
25 2 Inch Meter	147.70
3 Inch Meter	284.20
26 4 Inch Meter	479.20
6 Inch Meter	966.70
WIFA Surcharge	6.92
27 Sprinkler Rate	(a)

28 Commodity Charge – per 1,000 gallons	\$ 4.00
CAP Recovery Fee – per 1,000 gallons	\$ 0.32

SERVICE AND METER INSTALLATION CHARGE

Refundable pursuant to A.A.C. R14-2-405

5/8 x 3/4 Inch Meter	\$ 400.00
3/4 Inch Meter	440.00
1 Inch Meter	500.00
1 1/2 Inch Meter	675.00
2 Inch Meter - Compound	1,660.00
3 Inch Meter - Compound	2,150.00
4 Inch Meter - Compound	3,135.00
6 Inch Meter - Compound	6,190.00

SERVICE CHARGES

Establishment	25.00
Establishment - After Hours	50.00
Reconnection (Delinquent)	30.00
Reconnection (Delinquent/After Hours)	35.00
NSF Check	25.00
Meter Reread (If correct)	15.00
Meter Test (If correct)	30.00
Deposit	(b)
Deposit Interest	(b)
Re-Establishment (Within 12 months)	(c)
Re-Establishment (Within 12 months After Hours)	(d)
Deferred Payment - Per Month	1.50%
Late Payment Penalty - Per Month	1.50%
Moving Customer Meter (Customer Request)	Cost
Illegal Hook-up	(e)
Transfer Fee	25.00

(a) Higher of \$5.00 per month or 1.0 percent of monthly minimum

(b) Per Commission rule A.A.C. R14-2-403(B)

(c) Months off system time monthly minimum per A.A.C. R14-2-403(D)

(d) Months off system time monthly minimum per A.A.C. R14-2-403(D), plus \$25.00

(e) Estimated billings from time illegal connection was made to date

IT IS FURTHER ORDERED that Vail Water Company shall file a CAP Hook-up Fee Tariff that conforms to the Tariff Schedule contained in the Engineering Staff Report filed in this proceeding. The CAP Hook-up Fee shall be effective on the north system as of the effective date of this Order and applicable to the entire system after the interconnection of the north and south systems is complete.

IT IS FURTHER ORDERED that such rates and charges shall be effective for all usage on and after May 1, 2000.

IT IS FURTHER ORDERED that Vail Water Company shall notify its customers of the increased rates and charges authorized herein and the effective date of same as part of its next regularly scheduled billing.

1 IT IS FURTHER ORDERED that Vail Water Company shall file a copy of the notice of rates  
2 and charges approved herein and sent to its customers with the Director of the Utilities Division  
3 within 30 days from the effective date of this notice.

4 IT IS FURTHER ORDERED that Vail Water Company is authorized to borrow from the  
5 Water Infrastructure Finance Authority of Arizona up to \$644,000 for 20 years at an annual interest  
6 rate of 6.2550 percent and up to \$58,430 from shareholders for a term of 20 years at an annual  
7 interest rate of 10.25 percent.

8 IT IS FURTHER ORDERED that Vail Water Company is hereby authorized to engage in any  
9 transactions and to execute any documents necessary to effectuate the authorization granted herein  
10 above.

11 IT IS FURTHER ORDERED that such financing authority shall be expressly contingent upon  
12 Vail Water company's use of the proceeds for the purposes set forth in the finance application.

13 IT IS FURTHER ORDERED that approval of the financing set forth herein above does not  
14 constitute or imply approval or disapproval by the Commission of any particular expenditure of the  
15 proceeds derived thereby for purposes of establishing just and reasonable rates.

16 IT IS FURTHER ORDERED that Vail Water Company shall file with the Director of the  
17 commission's Utilities Division within 30 days of finalization, a copy of all loan documents which  
18 sets forth the terms of the proposed long-term debt if not previously filed.

19 IT IS FURTHER ORDERED that Vail Water Company shall comply with the  
20 recommendations, as modified, set forth in Findings of Fact Nos. 25, 26, 27 and 29.

21 IT IS FURTHER ORDERED that the WIFA surcharge approved herein shall be deposited  
22 into a segregated interest bearing account and used solely to repay the WIFA indebtedness and shall  
23 be interim and subject to refund in the event Vail Water Company fails to complete the  
24 improvements set forth in its finance application by September 1, 2001.

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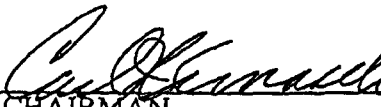
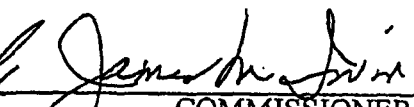
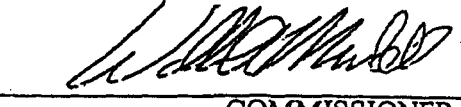
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1 IT IS FURTHER ORDERED that Vail Water Company shall file a rate case no earlier than  
2 twelve months or longer than eighteen months after the completion of the plant to be installed  
3 pursuant to this Order.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

6  
7     
8 CHAIRMAN COMMISSIONER COMMISSIONER  
9

10 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive  
11 Secretary of the Arizona Corporation Commission, have  
12 hereunto set my hand and caused the official seal of the  
13 Commission to be affixed at the Capitol, in the City of Phoenix,  
14 this 14th day of April, 2000.

15   
16 BRIAN C. McNEIL  
17 EXECUTIVE SECRETARY

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1 SERVICE LIST FOR:

VAIL WATER COMPANY

2 DOCKET NOS.

W-01651B-99-0351

W-01651B-99-0406

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BEFORE THE ARIZONA CORPORATION COMMISSION

GARY PIERCE  
Chairman

BOB STUMP  
Commissioner

SANDRA D. KENNEDY  
Commissioner

PAUL NEWMAN  
Commissioner

BRENDA BURNS  
Commissioner

IN THE MATTER OF THE APPLICATION OF )  
VAIL WATER COMPANY FOR AUTHORITY TO )  
ISSUE PROMISSORY NOTE(S) AND OTHER )  
EVIDENCE OF INDEBTEDNESS PAYABLE AT )  
PERIODS OF MORE THAN TWELVE MONTHS )  
AFTER THE DATE OF ISSUANCE. )

DOCKET NO. W-01651B-99-0351

IN THE MATTER OF THE APPLICATION OF )  
VAIL WATER COMPANY FOR A RATE )  
INCREASE )

DOCKET NO. W-01651B-99-0406

DIRECT

TESTIMONY

OF

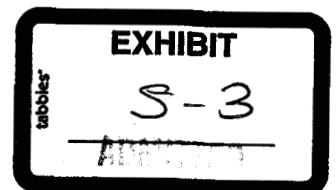
BRIAN K. BOZZO

COMPLIANCE AND ENFORCEMENT MANAGER

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

JANUARY 23, 2011



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**EXECUTIVE SUMMARY  
VAIL WATER COMPANY.  
DOCKET NO. W-01651B-99-0351  
DOCKET NO. W-01651B-99-0406**

Vail Water Company ("Company" or "Vail") is a public service corporation engaged in the business of providing public utility water service in Pima County.

The purpose of my testimony is to present Staff's position on certain compliance and enforcement issues relating to Decision No. 62450 and specifically to Finding of Fact 25 within the decision.

The Company was ordered to have final plans for direct use of Central Arizona Project ("CAP") water no later than December 31, 2010. Vail failed to meet that compliance requirement and the decision therefore required that all CAP charges would cease and that monies remaining in the CAP account would be refunded.

On August 19, 2011, after being contacted by Staff, the Company then sought an extension of time to comply with the final plans requirement. Staff reviewed the application and ultimately recommended denial of that request. Staff's position is that the Commission order was clear regarding the cessation of CAP collections and the refunding of remaining CAP monies.

1   **INTRODUCTION**

2   **Q.   Please state your name and business address.**

3   A.   My name is Brian K. Bozzo. My business address is 1200 West Washington Street,  
4       Phoenix, Arizona 85007.

5  
6   **Q.   By whom are you employed and in what capacity?**

7   A.   I am employed by the Arizona Corporation Commission ("Commission" or "A.C.C.") in  
8       the Utilities Division ("Staff") as the Compliance and Enforcement Manager.

9  
10   **Q.   Please describe your education and work experience.**

11   A.   I obtained a Bachelor of Science degree in Business Administration from the University of  
12       Arizona. In 1991, I joined Staff as a rate analyst. I have been responsible for conducting  
13       case preparation/analysis and serving as a Commission witness in rate proceedings,  
14       finance authorizations and Certificate of Convenience and Necessity ("CC&N")  
15       proceedings, among others. During the course of these duties, I attended numerous  
16       seminars on utility rate-making including courses presented by the National Association of  
17       Regulatory Utility Commissioners ("NARUC") and New Mexico State University.

18  
19       Since July 2003, I have been the manager of Compliance and Enforcement in the  
20       Compliance Section of the Utilities Division. In the course of these duties, I conduct  
21       analyses of numerous compliance matters, document compliance findings and make  
22       recommendations on compliance status.  
23

1     **Q.     In general, what is the responsibility of the Compliance Section of the Utilities**  
2     **Division in the Commission?**

3     A.     Compliance is the section within the Utilities Division of the Commission that is devoted  
4     to the identification, collection and documentation of company filings ordered by the  
5     A.C.C.

6  
7     **Q.     What is the purpose of your testimony in this proceeding?**

8     A.     The purpose of my testimony is to present Staff's position on certain compliance and  
9     enforcement issues ordered in Decision No. 62450, to comment on Vail Water Company's  
10    ("Company" or "Vail") continuing request for an extension of time and, specifically, to  
11    address the cessation of Central Arizona Project ("CAP") fees and the refunding of  
12    remaining CAP funds as outlined in Finding of Fact ("FOF") 25 within the decision.

13  
14    **Q.     Are the nature and dates of Vail Water Company's compliance filings within the**  
15    **scope of your duties?**

16    A.     Yes. The Compliance section monitors and tracks Compliance ordered by the  
17    Commission and the Compliance filings ordered in Decision No. 62450 are a subset of the  
18    overall compliance ordered by the Commission.

19  
20    **Q.     In the scope of your duties, do you communicate compliance status and complete**  
21    **testimony, Complaints or Order to Show Cause ("OSC") filings on the compliance**  
22    **status of Arizona utility companies?**

23    A.     Yes. I have composed and presented various work documents regarding compliance on  
24    Arizona utility firms. In addition, one of the major responsibilities of the Compliance  
25    Section is providing information on the compliance ordered by the Commission and on the  
26    Company performance in meeting those Commission requirements.

1 **Q. Are the Staff members who originally conducted the casework on this item currently**  
2 **employed at the Commission?**

3 A. No. Given the 1999 docket date, the individuals originally assigned to the matter are no  
4 longer employed by the Commission. I was assigned to this matter to provide Staff's  
5 current testimony in lieu of those individuals. Although I did not work on this matter  
6 originally, I did author the October 31, 2011 Staff response to the Company request for  
7 extension of time.

8  
9 **JANUARY 26<sup>TH</sup> HEARING**

10 **Q. What is your understanding of the specific purpose of the January 26, 2012 hearing?**

11 A. The purpose of the initial hearing is to present direct and rebuttal testimony and discuss  
12 the issues surrounding the question of "whether CAP funds currently held in trust may be  
13 used to make CAP payments due in March 2012."

14  
15 **Q. Does the language in Decision No. 62450 suggest that Vail should be allowed use the**  
16 **CAP funds to make a CAP payment due in March 2012?**

17 A. No. FOF 25 in Decision No. 62450 is very clear on this issue. Pursuant to Decision No.  
18 62450, Vail was ordered to comply with individual ordering paragraphs in Finding of Fact  
19 ("FOF") 25(f), 25(g) and 25(j). Those FOF 25 sections read as follows:

20  
21 (f) *"Final plans for the direct use of CAP water within Vail's service territory*  
22 *are to be submitted to the Commission no later than December 31, 2010."*

23  
24 (g) *"Vail must directly use the CAP allocation within its service territory by*  
25 *December 31, 2015."*

26  
27 (j) *"If Vail does not comply with either of the timeframes in f or g, all CAP*  
28 *charges will cease at that time and any monies remaining in the CAP account*  
29 *shall be refunded in a manner to be determined by the Commission at that*  
30 *time;"*

1 **Q. Consistent with FOF 25(f), did the Company comply with the requirement to submit**  
2 **"final plans" by December 31, 2010?**

3 A. No. The Company failed to meet the Commission requirement and has admitted that fact  
4 before the Commissioners in Open Meeting.  
5

6 **Q. Discuss the ramifications of failing to comply with FOF 25(f).**

7 A. The ramifications are clear and significant. Having failed to comply with the requirement  
8 to provide "final plans" associated with FOF 25(f), the Company was, on January 1, 2011,  
9 subject to the conditions of FOF 25(j) which requires that all CAP charges cease and  
10 remaining CAP account monies be refunded.  
11

12 **Q. Since Decision No. 62450 stated that the monies must be refunded, should they be**  
13 **used by Vail to make a March 2012 CAP payment?**

14 A. No. Staff believes that the upcoming CAP bill should be paid with other funds and the  
15 remaining CAP monies should be refunded to customers in accordance with Decision No.  
16 62450.  
17

18 **FEBRUARY 29TH HEARING**

19 **Extension of time**

20 **Q. Has Staff provided a memorandum regarding the Company's original request for**  
21 **extension of time?**

22 A. Yes. On November 1, 2011, Staff docketed a memorandum responding to the Company  
23 request for extension of time. I authored that memorandum which provided information  
24 about the Company performance regarding Decision No. 62450 and the manner in which  
25 the Company came to apply for their extension of time. Staff recommended denial of the  
26 Company request for extension of time.



1 **Q. In spite of Staff's denial recommendation, is the Company currently seeking**  
2 **consideration for an extension of time in this matter?**

3 A. Yes.

4  
5 **Q. Did the Company docket a request for extension of time at any time prior to the**  
6 **"final plans" requirement due date of December 31, 2010?**

7 A. No.

8  
9 **Q. Did the Company proactively contact Staff after the "final plans" were delinquent in**  
10 **January 2011 to inform Staff of the delinquency, of the impact of the FOF 2(j)**  
11 **language and of the requirement to cease CAP collections and refund CAP monies?**

12 A. No. Staff was the party that identified that the Company had failed to meet the "final  
13 plans" requirement and ultimately informed the Company that it was in violation of  
14 Decision No.62450. Frankly, it is unclear when or if the Company would have addressed  
15 the issue if it had not been notified by Staff of being in violation of the decision.

16  
17 **Q. Please discuss how Staff notified the Company about these issues.**

18 A. On June 21, 2011, Staff sent a formal Compliance Notification Letter stating that the  
19 Company had failed to meet the Commission requirement of making the "Final plans"  
20 filing by December 31, 2010. This Letter notified the Company that its failure to meet the  
21 Commission deadline rendered the Company in violation of Decision No. 62450. Staff's  
22 Compliance Notification Letter also notified the company of FOF 25 (j) which states that  
23 that CAP charges should cease and remaining monies be refunded when the Company  
24 failed to timely provide the "Final plans" filing in FOF 25 (f).

25

1 **Q. Did Staff provide Vail with a second Compliance letter on this issue?**

2 A. Yes. On August 2, 2011, Staff sent a second letter titled Compliance Status Notification #  
3 2 to reiterate the collection and refunding obligations of CAP charges found in Decision  
4 No. 62450's FOF 25 (j). The second letter advised the Company of the following:

5 *"... consistent with Finding of Fact 25 (j), the Company should immediately*  
6 *cease CAP collections and propose to the Commission a mechanism to refund*  
7 *any monies remaining in the CAP account. This proposal should be submitted*  
8 *to the Commission by August 19, 2011. Further the Company is notified that*  
9 *any CAP funds collected since January 1, 2011 were collected in violation of*  
10 *a Commission order."*  
11  
12

13 **Q. Did the Company comply with Staff's August 19, 2011 deadline for providing the**  
14 **proposed refunding mechanism?**

15 A. No.  
16

17 **Q. Did the Company make another filing on August 19, 2011?**

18 A. Yes. On August 19, 2011, the Company chose to docket an extension of time request  
19 titled "Application To Extend Time For CAP Planning".  
20

21 **Q. Please summarize Staff's position on the Company performance in this regard.**

22 A. The following outlines the Company performance prior to Staff identifying and notifying  
23 the Company of its delinquency and violation of Decision No.62450:

- 24 • The Company failed to docket a request for extension of time in a timely manner  
25 (prior to the required due date).
- 26 • The Company failed to file the "final plans" by the December 31, 2010 due date as  
27 ordered by Decision No. 62450.
- 28 • The Company failed to identify its own delinquency and the subsequent  
29 ramifications of the delinquency during almost the entire first half of 2011.

- The Company failed to notify Staff of the delinquency and Decision No. 62450 enforcement language.
- The Company failed to cease collection of CAP charges per Decision No. 62450.
- The Company failed to refund the remaining monies in the CAP account.

**Q. Does Staff's position preclude the Company from continuing the CAP water plan?**

A. No.

**Q. What other options does or did Vail have for assuring funds exist or existed for pursuing the CAP water goal?**

A. The Company could long ago have docketed an application for a rate increase and/or docketed an application for financing and/or sought to assure that adequate shareholder funds existed to fund the CAP plan. Staff's concern is that the Company has been consistently been reactive rather than proactive regarding these administrative and planning requirements that are/were necessary to meet the CAP water goal.

**Q. If the Commission grants an extension of time to Vail in this proceeding, is there any condition that should be included in the Commission decision?**

A. Yes. Because of the extension of time and the potential effect of the CAP issue on the Company, if the Commission grants an extension of time it should also order Vail to file a rate application within 60 days of a Commission decision in this matter.

**Q. Is Staff changing its recommendation provided in the November 1, 2011 Staff memorandum which responded to the Company request for extension of time?**

A. No. Staff continues to recommend that the Company's performance in the matter does not warrant the Commission granting an extension of time. In summary, the funding set forth

1 in Decision No. 62450 for financing the CAP water project is now forfeit by the  
2 Company. The current decision cannot fund CAP water plans as those monies should be  
3 refunded to customers. In the absence of some modifying decision, the Company should  
4 utilize alternate funds to finance the CAP project.

5  
6 **Decision No. 62450 Language**

7 **Q. Has any question been raised about the language in Decision No. 62450?**

8 A. Yes. The Company attorney pointed out to Staff that FOF 7 within the Conclusions of  
9 Law section of the decision does not correspond with the ordering paragraph and/or FOF  
10 25 language that Staff discussed in its extension of time memorandum on November 1,  
11 2011.

12  
13 **Q. Please highlight the relevant language in the ordering section and FOF 25(h) and**  
14 **FOF 25(k) of Decision No. 62450.**

15 A. That information is as follows, with the ordering paragraph shown first and FOF 25(h) and  
16 25(k) following:

17 *"IT IS FURTHER ORDERED that Vail Water Company shall comply with the*  
18 *recommendations, as modified, set forth in Findings of Fact Nos. 25, 26, 27*  
19 *and 29.*

20 (h) *"No time extensions will be allowed for any reason."*

21  
22 (k) *"The Commission shall allow Staff to automatically impose fines*  
23 *and/or other sanctions against Vail if the timeframes in item f or g are*  
24 *not met;"*

25  
26 **Q. Please highlight the relevant language in the "conclusions of law" section of Decision**  
27 **No. 62450 to which the Company attorney was referring.**

28 A. That language is as follows:

1                   *"Staff's recommendations set forth in Findings of Fact Nos. 25, 26, 27 and 29*  
2                   *and Finding of Fact No. 28 are reasonable, except that paragraph 25k is not*  
3                   *warranted and pursuant to paragraph 25d, funds collected from the CAP*  
4                   *Hook-up Fees may be used for CAP-related capital projects; and paragraph*  
5                   *25h should be modified to provide no time extensions will be allowed absent a*  
6                   *showing of good cause."*

7  
8   **Q.     Please summarize the issue relating to this language.**

9   A.     Staff's November 1, 2011 memorandum stated that the Commission order approved FOF  
10         25(h) and FOF 25(k). However, the ordering paragraph states that the Company should  
11         comply with the FOF's "as modified" and the Company believes the language in the  
12         "Conclusion of Law" section is the modification referred to in the ordering paragraph.

13  
14   **Q.     Was this language issue identified by any party in the previous meetings with the**  
15         **Commission?**

16   A.     No, I do not recall this language issue mentioned previously.

17  
18   **Q.     Is the language in the "Conclusion of Law" section actually the modification referred**  
19         **to in the decision's ordering paragraph?**

20   A.     I was not involved in the original casework in this matter to know with any certainty, but,  
21         since the ordering paragraph includes the words "as modified" and the "Conclusions of  
22         Law" section has language that essentially modifies FOF 25(h) and FOF 25(k), it appears  
23         that could be the modification referenced.

24

1 **Q. What is the result of this modification issue to Staff's position?**

2 A. This issue relates to FOF 25(h) and FOF 25(k) of Decision No. 62450. The first result of  
3 the modification language issue is that FOF 25(k) was "not warranted" and is not ordered  
4 by the Commission. Therefore, Staff could not automatically impose fines and/or other  
5 sanctions against Vail. The second result is that FOF 25(h) would be modified such that  
6 no time extensions would be allowed *absent a showing of good cause*.

7  
8 **Q. Did Staff automatically impose fines and/or other sanctions against Vail in its**  
9 **November 1, 2011 Staff response memorandum to the Company request for**  
10 **extension of time?**

11 A. No. Staff did not. Staff did reserve the right to make further recommendations to the  
12 Commission regarding fines and sanctions but made no automatic "fines or other  
13 sanctions" of its own.

14  
15 **Q. Staff originally interpreted FOF 25(h) as stating that extension of time would not be**  
16 **allowed "for any reason" rather than "absent a showing of good cause". Was the**  
17 **original interpretation the reason for denying the extension of time?**

18 A. No. It was presented as one item amongst many - as shown on page one and in the  
19 summary section of the November 1, 2011 Staff response memorandum.

20  
21 **Q. What was the basis of Staff's denial of the Company request for extension of time in**  
22 **Staff's November 1, 2011 memorandum?**

23 A. Staff's summary and recommendation section read as follows:

24  
25 ~~"In summary, a review of this matter indicates that Vail is in violation of~~  
26 ~~Commission Decision No. 62450 via the failure to provide "Final plans",~~  
27 ~~failure to cease collection of CAP charges and failure to refund monies~~  
28 ~~remaining in the CAP account. The Company is also in violation of Arizona~~

1 Revised Statute §40-202 and Staff's enforcement efforts to receive a  
2 Company filing on a proposed refunding mechanism. Staff concludes that the  
3 facts in this matter preclude it from recommending an extension of time in this  
4 case.

5  
6 Also, Staff notes that there was no extension of time request made prior to the  
7 December 31, 2010 due date in this matter. Staff is concerned that the request  
8 for extension of time was filed approximately 6 months after the due date on  
9 this ten year old requirement and then only after Staff notified the Company  
10 of the compliance violation.

11  
12 Based on all of the above, Staff recommends denial of the Company's request  
13 for extension of time for provision of the "Final plans" filing outlined in  
14 Decision No. 62450.  
15

16 **Q. Does Staff believe that the summary listed above shows good cause for not**  
17 **granting a time extension?**

18 **A. Yes.**  
19

20 **Q. In total, does the issue of the modification language change Staff's**  
21 **recommendation regarding this matter?**

22 **A. No.**  
23

24 **Q. Does this conclude your direct testimony regarding the Vail Water Company**  
25 **rehearing matter?**

26 **A. Yes, it does.**  
27

**ORIGINAL**  
**MEMORANDUM**

TO: Docket Control Center

FROM: Steven M. Olea  
Director  
Utilities Division

DATE: October 31, 2011

RE: VAIL WATER COMPANY (DOCKET NOS. W-016518-99-0351 AND W-016518-99-0406)

Arizona Corporation Commission

**DOCKETED**

NOV 1 2011

DOCKETED BY

*[Signature]*

**RECEIVED**

2011 NOV -1 A 8:23

AZ CORP COMMISSION  
DOCKET CONTROL

In Decision No. 62450, dated April 14, 2000, the Arizona Corporation Commission ("Commission") approved the application of Vail Water Company ("Vail" or "Company") for a rate increase and authority for financing.

**Compliance Requirements and Enforcement Letters**

Pursuant to Decision No. 62450, Vail was ordered to comply with Finding of Fact ("FOF") 25 within the decision. Specifically, in FOF 25 (f), (g), (h), (j) and (k) the Commission ordered that:

- (f) ***"Final plans for the direct use of CAP water within Vail's service territory are to be submitted to the Commission no later than December 31, 2010."***
- (g) ***"Vail must directly use the CAP allocation within its service territory by December 31, 2015."***
- (h) ***"No time extensions will be allowed for any reason."***
- (j) ***"If Vail does not comply with either of the timeframes in f or g, all CAP charges will cease at that time and any monies remaining in the CAP account shall be refunded in a manner to be determined by the Commission at that time;"***
- (k) ***"The Commission shall allow Staff to automatically impose fines and/or other sanctions against Vail if the timeframes in item f or g are not met;"***

Based on its compliance review, Staff concluded that the Company did not comply with the above Commission requirement 25 (f) to provide the "Final plans" by the December 31, 2010 due date. Staff contacted the Company about the required filing and spoke with Mr. Christopher T. Volpe, Vice President, who confirmed that the "Final plans" had not been submitted.

On June 21, Staff sent a formal Compliance Notification Letter stating that the Company had failed to meet the Commission requirement of making the "Final plans" filing by December 31, 2010. This Letter notified the Company that its failure to meet the Commission deadline rendered the

**EXHIBIT**

*S-4*



Company in violation of both Decision No. 62450 and Arizona Revised Statute ("A.R.S.") §40-202 which requires the Company to comply with every "order, decision, rule or regulation" of the Commission. Staff's Compliance Notification Letter also notified the company of FOF 25 (j) which states that that CAP charges should cease and remaining monies refunded when the Company failed to timely provide the "Final plans" filing in FOF 25 (f). For further information, please see Staff's June 21, 2011 Letter which is attached to this memorandum for reference purposes.

On August 2, 2011, Staff sent a second letter titled Compliance Status Notification #2 to reiterate the collection and refunding obligations of CAP charges found in Decision No. 62450's FOF 25 (j). This second letter is also attached to this memorandum and advised the Company of the following:

***"... consistent with Finding of Fact 25 (j), the Company should immediately cease CAP collections and propose to the Commission a mechanism to refund any monies remaining in the CAP account. This proposal should be submitted to the Commission by August 19, 2011. Further the Company is notified that any CAP funds collected since January 1, 2011 were collected in violation of a Commission order."***

The Company did not comply with Staff's deadline for providing the proposed refunding mechanism.

#### **Requests for Extension of Time**

On June 30, 2011, in response to Staff's June 21, 2011 initial Compliance letter, the Company submitted a single page letter requesting an extension of time until November 30, 2011, for the provision of the "Final plans". This request for extension of time was ultimately withdrawn by the Company in a letter docketed on August 17, 2011.

On August 19, 2011, Vail docketed a subsequent request for extension of time until June 30, 2013 to provide the "Final plans" for direct use of CAP water. In its application, the Company suggests that while the City of Tucson Water Department ("the City") had the intention of "becoming a wholesale CAP delivery utility", this did not happen. Only recently, in June 2011, did the City and the Town of Oro Valley execute an "intergovernmental agreement for wheeling CAP water that the City anticipates will serve as a model for providing similar services" to other firms such as the Company. The Company is now "entirely confident" that it can reach a wheeling agreement with the City which will allow them to make direct use of CAP water in its service territory.

The application states that a great deal of money has been spent attempting to make a renewable water supply available but the City was not previously available as a "willing partner to wheel CAP water across the Tucson valley". Given that the direct use of CAP remains the Company's preferred goal, and based on what the Company calls a "new water policy regime in effect" at the City, Vail requests that the December 31, 2010 deadline for the provision of "Final plans" for direct use of CAP water be extended until **June 30, 2013**.

**Summary and Recommendation**

In summary, a review of this matter indicates that Vail is in violation of Commission Decision No. 62450 via the failure to provide "Final plans", failure to cease collection of CAP charges and failure to refund monies remaining in the CAP account. The Company is also in violation of Arizona Revised Statute §40-202 and Staff's enforcement efforts to receive a Company filing on a proposed refunding mechanism. Staff concludes that the facts in this matter preclude it from recommending an extension of time in this case.

Also, Staff notes that there was no extension of time request made prior to the December 31, 2010 due date in this matter. Staff is concerned that the request for extension of time was filed approximately 6 months after the due date on this ten year old requirement and then only after Staff notified the Company of the compliance violation.

Based on all of the above, Staff recommends denial of the Company's request for extension of time for provision of the "Final plans" filing outlined in Decision No. 62450. In order to clarify and enhance the record, Staff further recommends that Vail docket a status update by November 15, 2011 clarifying the following:

- Whether the Company has ceased collecting CAP charges and an explanation why not, if not.
- What refunding mechanism the Company proposes and why none was proposed by Staff's due date.
- Whether refunds have started and an explanation why not, if not.
- An accounting of the total amount of funds in the CAP account to be refunded.

Finally, regarding the fines and other sanctions mentioned in FOF 25 (k), Staff reserves the right to make further recommendations based on the quality and timeliness of the Company's November 15, 2011 status update.

SMO:BKB:lm

Originator: Brian K. Bozzo

Attachments

SERVICE LIST FOR:  
DOCKET NO.

VAIL WATER COMPANY  
DOCKET NOS. W-01651A-99-0351 & W-01651A-99-0406

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COMMISSIONERS  
GARY PIERCE - Chairman  
BOB STUMP  
SANDRA D. KENNEDY  
PAUL NEWMAN  
BRENDA BURNS



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COMPLIANCE  
NOTIFICATION  
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W-016518-99-0351  
W-016518-99-0406

June 21, 2011

Arizona Corporation Commission  
DOCKETED

AUG 2 2011

CERTIFIED MAIL

Mr. Christopher T. Volpe  
Vice President  
Vail Water Company  
1010 North Finance Center Drive, Suite 200  
Tucson, Arizona 85710

DOCKETED BY	
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RE: VAIL WATER COMPANY - COMPLIANCE STATUS NOTIFICATION  
DECISION NO. 62450

In Decision No. 62450, dated April 14, 2000, the Arizona Corporation Commission ("A.C.C." or "the Commission") approved Finding of Fact 25(f), which included the following order of the Commission:

*"Final plans for the direct use of CAP water within Vail's service territory are to be submitted to the Commission no later than December 31, 2010."*

Based on previous year annual reports and on the most recent June 14, 2011 annual report update provided by the Company, Vail Water Company ("Vail" or "Company") remains to this day in the same status of "investigating alternative plans" for CAP water use. This status extends all the way back to the year of 2004 and prior.

As such, the Company has not, as of this date, provided the "final plans" for direct use of CAP water and is therefore considered in violation of Decision No. 62450. Failure to comply with the decision further places the Company in violation of Arizona Revised Statute ("A.R.S.") §40-202, which states:

*"A public service corporation shall comply with every order, decision, rule or regulation made by the commission in any matter relating to or affecting its business as a public service corporation, and shall do everything necessary to secure compliance with and observance of every such order, decision, rule or regulation."*

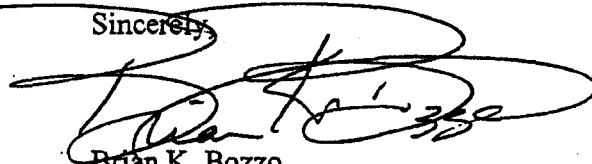
The Company has previously dealt with Compliance Staff via telephone regarding this matter. This writing is meant to formally notify Vail that the Company has not met the required compliance that was ordered by the Commission. The Company should do so immediately.

Vail Water Company  
Compliance Status Letter  
June 21, 2011  
Page 2

Finally, the Company is further notified that Decision No. 62450 also sets forth that all CAP charges will cease and remaining CAP monies shall be refunded in the event that the Company fails to meet the requirements of the decision.

If you believe our conclusions are in error, please submit a detailed explanation as to why you believe Staff's conclusions are in error. Please submit this explanation by July 1, 2011. You may also contact the Utilities Division at (602) 542-4251 or reach me at (602) 542-0852 if you require any further information.

Sincerely,

A handwritten signature in black ink, appearing to read "Brian K. Bozzo", with a large, sweeping flourish extending to the left.

Brian K. Bozzo  
Compliance and Enforcement Manager  
Utilities Division

BKB:lhnm

ORIGINAL

COMMISSIONERS  
GARY PIERCE - Chairman  
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SANDRA D. KENNEDY  
PAUL NEWMAN  
BRENDA BURNS



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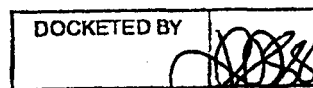
Arizona Corporation Commission

DOCKETED

AUG 2 2011

August 2, 2011

Mr. Christopher T. Volpe  
Vice President  
Vail Water Company  
1010 N. Finance Center Dr., Suite 200  
Tucson, Arizona 85710



RE: VAIL WATER COMPANY - COMPLIANCE STATUS NOTIFICATION #2  
DOCKET NOS. W-01651B-99-0351 & W-01651B-99-0406  
DECISION NO. 62450

On June 22, 2011, Staff issued a letter (Compliance Notification) informing Vail Water Company ("Company") of its obligation to comply with Commission Decision No. 62450, dated April 14, 2000. Pursuant to this order, Findings of Fact 25(f), 25(g) and 25(j) respectively, state:

- (f) *"Final plans for the direct use of CAP water within Vail's service territory are to be submitted to the Commission no later than December 31, 2010;"*
- (g) *"Vail must directly use the CAP allocation within its service territory by December 31, 2015;"*
- (j) *"If Vail does not comply with either of the timeframes in f or g, all CAP charges will cease at that time and any monies remaining in the CAP account shall be refunded in a manner to be determined by the Commission at that time;"*

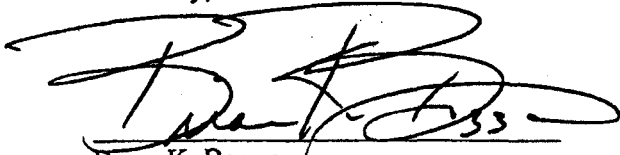
As stated in the June 22, 2011 letter, the Company has failed to comply with Finding of Fact 25(f) of Decision No. 62450 and this current letter serves as a second notification and a reminder that the Company has failed to meet that deadline associated with the "final plans" requirement.

In our previous telephone conversation, you stated that the Company has neither ceased collecting nor refunded the referenced Central Arizona Project ("CAP") monies. This letter is to advise you that, consistent with Finding of Fact 25(j), the Company should immediately cease CAP collections and propose to the Commission a mechanism to refund any monies remaining in the CAP account. This proposal should be submitted to the Commission by August 19, 2011. Further, the Company is notified that any CAP funds collected since January 1, 2011 were collected in violation of a Commission order.

Vail Water Company  
Compliance Status Letter # 2  
Page 2

If you have any questions, please feel free to contact me at (602) 542-0852.

Sincerely,

A handwritten signature in black ink, appearing to read "Brian K. Bozzo", written over a horizontal line.

Brian K. Bozzo  
Compliance and Enforcement Manager